

EATON CORP
Form S-3ASR
February 24, 2012
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As filed with the Securities and Exchange Commission on February 24, 2012

Registration No. 333-

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM S-3

REGISTRATION STATEMENT

Under

the Securities Act of 1933

Eaton Corporation

(Exact name of Registrant as specified in its charter)

Ohio

(State or other Jurisdiction of Incorporation or Organization)

34-0196300

(IRS Employer Identification No.)

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Eaton Center, 1111 Superior Avenue, Cleveland, Ohio 44114-2584, (216) 523-5000

(Address, including Zip Code, and Telephone Number, including Area Code, of Registrant's Principal Executive Offices)

THOMAS E. MORAN, Senior Vice President and Secretary

Eaton Corporation, Eaton Center, 1111 Superior Avenue, Cleveland, Ohio 44114-2584, (216) 523-4103

(Address, including Zip Code, and Telephone Number, including Area Code, of Agent for Service)

Copy to:

LISA L. JACOBS

Shearman & Sterling LLP, 599 Lexington Avenue, New York, New York 10022

Approximate date of commencement of proposed sale of the securities to the public: From time to time after the effective date of this Registration Statement.

If the only securities being registered on this Form are being offered pursuant to dividend or interest reinvestment plans, please check the following box.

If any of the securities being registered on this Form are to be offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act of 1933, other than securities offered only in connection with dividend or interest reinvestment plans, check the following box.

If this Form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, please check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering.

If this Form is a post-effective amendment filed pursuant to Rule 462(c) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering.

If this Form is a registration statement filed pursuant to General Instruction I.D. or a post-effective amendment thereto that shall become effective upon filing with the Commission pursuant to Rule 462(e) under the Securities Act, check the following box.

If this Form is a post effective amendment to a registration statement filed pursuant to General Instruction I.D. filed to register additional securities or additional classes of securities pursuant to Rule 413 (b) under the Securities Act, check the following box.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Securities Exchange Act of 1934.

Large accelerated filer

Accelerated filer

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Non-accelerated filer (Do not check if a smaller reporting company)

Smaller reporting company

CALCULATION OF REGISTRATION FEE

Title of Each Class of Securities to be Registered	Amount to be Registered(1)	Proposed Maximum Offering Price Per Unit(1)	Proposed Maximum Aggregate Offering Price(1)	Amount of Registration Fee(1)
Debt Securities				
Preferred Shares				
Common Shares, par value \$0.50 per share				
Warrants				
Units(2)				

- (1) An indeterminate aggregate initial offering price or number of securities of each identified class is being registered as may from time to time be offered at indeterminate prices. Separate consideration may or may not be received for securities that are issuable on exercise, conversion or exchange of other securities or that are issued in units. In accordance with Rules 456(b) and 457(r), the Registrant is deferring payment of all of the registration fee.
- (2) Each unit will be issued under a unit agreement or indenture and will represent an interest in one or more debt securities, preferred shares, common shares and warrants as well as debt or equity securities of third parties, in any combination, which may or may not be separable from one another.

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Eaton Corporation

Senior Debt Securities

Preferred Shares

Common Shares

Warrants

Units

We may offer and sell, from time to time, in one or more offerings, senior debt securities, preferred shares, common shares and warrants, as well as units that include any of these securities or securities of other entities. The debt securities, preferred shares and warrants may be convertible into or exercisable or exchangeable for common or preferred shares or other securities of the Company or debt or equity securities of one or more other entities. We may offer and sell these securities to or through one or more underwriters, dealers and agents, or directly to purchasers, on a continuous or delayed basis.

The specific terms of any securities to be offered will be described in a prospectus supplement or term sheet. You should read this prospectus and the accompanying prospectus supplement or term sheet carefully before you invest in our securities.

The common shares of the Company are listed on the NYSE and the Chicago Stock Exchange and trade under the ticker symbol **ETN**.

Investments in the securities involve certain risk. See **Risk Factors** beginning on page 3 of this prospectus.

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or passed upon the accuracy or adequacy of this prospectus. Any representation to the contrary is a criminal offense.

The date of this prospectus is February 24, 2012.

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ABOUT THIS PROSPECTUS

The information contained in this prospectus is not complete and may be changed. You should rely only on the information provided in or incorporated by reference in this prospectus, any prospectus supplement or other offering materials. We have not authorized anyone else to provide you with different information. We are not making an offer of any securities in any jurisdiction where the offer is not permitted. You should not assume that the information in this prospectus, any prospectus supplement, other offering materials or any document incorporated by reference is accurate as of any date other than the date of the document in which such information is contained or such other date referred to in such document, regardless of the time of any sale or issuance of a security.

This prospectus is part of a registration statement that we filed with the Securities and Exchange Commission (the SEC) using a shelf registration process. This prospectus contains a general description of the securities we may offer. Each time we sell or issue securities, we will provide a prospectus supplement or term sheet that will contain specific information about the terms of that offering and the manner in which they may be offered. The prospectus supplement or term sheet may also add to, update or change information contained in this prospectus. If so, the prospectus supplement or term sheet should be read as superseding this prospectus. You should read both this prospectus and any prospectus supplement or term sheet, together with additional information described under the heading **Where You Can Find More Information**, before making an investment decision. As used in this prospectus, the terms **we**, **us** and **our** refer to Eaton Corporation.

FORWARD LOOKING STATEMENTS

This prospectus, any prospectus supplement and the documents incorporated into this prospectus by reference contain forward-looking statements, as defined in Section 27A of the Securities Act of 1933, as amended (the Securities Act), and Section 21E of the Exchange Act. Statements that are not historical facts, including statements about beliefs and expectations, are forward-looking statements. These statements discuss potential risks and uncertainties and, therefore, actual results may differ materially. You are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date on which they are made. Eaton Corporation does not undertake any obligation to update any forward-looking statements, whether as a result of new information, future events or otherwise. Such forward-looking statements may include, without limitation, statements relating to the following:

projections of revenues, income, earnings per share, capital expenditures, dividends, capital structure, or other financial measures;

descriptions of anticipated plans or objectives of management for operations, products, or services;

forecasts of performance; and

assumptions regarding any of the foregoing.

Because these statements involve anticipated events or conditions, forward-looking statements often include words such as **anticipate**, **believe**, **can**, **could**, **estimate**, **expect**, **intend**, **may**, **plan**, **project**, **should**, **target**, **will**, **would**, or similar expressions.

By their very nature, forward-looking statements involve inherent risks and uncertainties, both general and specific, and risks exist that predictions, forecasts, projections and other outcomes described or implied in forward-looking statements will not be achieved. A number of important factors could cause results to differ materially from the plans, objectives, expectations, estimates and intentions expressed in such forward-looking statements.

Do not unduly rely on forward-looking statements. They represent our expectations about the future and are not guarantees. Forward-looking statements are only as of the date they are made, and, except as required by law, might not be updated to reflect changes as they occur after the forward-looking statements are made. We urge you to review Eaton Corporation's filings with the Securities and Exchange Commission for any updates to our forward-looking statements.

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WHERE YOU CAN FIND MORE INFORMATION

We file annual, quarterly and special reports, proxy statements and other information with the SEC. You may read and copy any document we file at the SEC's public reference room at 100 F Street, N.E., Washington D.C. 20549. Please call the SEC at 1-800-SEC-0330 for further information on its public reference room. Our SEC filings are also available to the public from the SEC's web site at <http://www.sec.gov>. Our common shares are listed on the New York Stock Exchange and the Chicago Stock Exchange and information about us also is available there.

This prospectus is part of a registration statement that we have filed with the SEC. The SEC allows us to incorporate by reference into this prospectus the information we file with it. This means that we can disclose important information to you by referring you to other documents separately filed with the SEC. The information incorporated by reference is considered to be part of this prospectus, unless and until that information is updated and superseded by the information contained in this prospectus or any information incorporated later. We incorporate by reference the documents listed below and any future filings we make with the SEC under Sections 13(a), 13(c), 14 or 15(d) of the Securities Exchange Act of 1934, as amended (the Exchange Act), until our offering of securities has been completed.

Annual Report on Form 10-K for the year ended December 31, 2011.

Information in our definitive proxy statement filed on March 18, 2011 under the captions "Election of Directors", "Section 16(a) Beneficial Ownership Reporting Compliance" and "Board Committees - Audit Committee."

Our filings with the SEC, including our Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, current reports on Form 8-K and amendments to those reports, are available free of charge on our website as soon as reasonably practicable after they are filed with, or furnished to, the SEC. Our internet website is located at <http://www.eaton.com>. The contents of the website are not incorporated by reference into this prospectus. You may also obtain a copy of these filings, at no cost, by writing to or telephoning us at the following address:

Eaton Corporation

Eaton Center

1111 Superior Avenue

Cleveland, Ohio 44114-2584

Attn: Shareholder Relations

(216) 523-5000

RISK FACTORS

Your investment in the securities involves certain risks. In consultation with your own financial and legal advisers, you should carefully consider whether an investment in the securities is suitable for you. The securities are not an appropriate investment for you if you do not understand the terms of the securities or financial matters generally. In addition, certain factors that may adversely affect the business of Eaton Corporation are discussed in our periodic reports referred to in "Where You Can Find More Information," above. For example, our Annual Report on Form 10-K for the year ended December 31, 2011 contains a discussion of significant risks that could be relevant to an investment in the securities. You should not purchase the securities described in this Prospectus unless you understand and know you can bear all of the investment risks involved.

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THE COMPANY

We are a diversified power management company with 2011 net sales of \$16 billion. We are a global technology leader in electrical components and systems for power quality, distribution and control; hydraulics components, systems and services for industrial and mobile equipment; aerospace fuel, hydraulics and pneumatic systems for commercial and military use; and truck and automotive drivetrain and powertrain systems for performance, fuel economy and safety. We have approximately 73,000 employees in over 50 countries and sell products to customers in more than 150 countries.

Operating segments are defined as components of an enterprise about which separate financial information is available that is evaluated on a regular basis by the chief operating decision maker, or decision making group, in deciding how to allocate resources to an individual segment and in assessing performance. Our segments are as follows:

Electrical Americas and Electrical Rest of World

The Electrical segments are global leaders in electrical components and systems for power quality, distribution and control. Products include circuit breakers, switchgear, UPS systems, power distribution units, panelboards, loadcenters, motor controls, meters, sensors, relays and inverters. The principal markets for the Electrical Americas and Electrical Rest of World segments are industrial, institutional, governmental, utility, commercial, residential and information technology. These products are used wherever there is a demand for electrical power in commercial buildings, data centers, residences, apartment and office buildings, hospitals, factories and utilities. The segments share several common global customers, but a large number of customers are located regionally and sales are made directly to original equipment manufacturers and indirectly through distributors, resellers and manufacturers representatives.

Hydraulics

The Hydraulics segment is a global leader in hydraulics components, systems and services for industrial and mobile equipment. Eaton offers a wide range of power products including pumps, motors and hydraulic power units; a broad range of controls and sensing products including valves, cylinders and electronic controls; a full range of fluid conveyance products including industrial and hydraulic hose, fittings, and assemblies, thermoplastic hose and tubing, couplings, connectors, and assembly equipment; filtration systems solutions; heavy-duty drum and disc brakes; and golf grips. The principal markets for the Hydraulics segment include oil and gas, renewable energy, marine, agriculture, construction, mining, forestry, utility, material handling, truck and bus, machine tools, molding, primary metals and power generation. Key manufacturing customers in these markets and other customers are located globally, and these products are sold and serviced through a variety of channels.

Aerospace

The Aerospace segment is a leading global supplier of aerospace fuel, hydraulics and pneumatic systems for commercial and military use. Products include hydraulic power generation systems for aerospace applications including, pumps, motors, hydraulic power units, hose and fittings, electro-hydraulic pumps and power and load management systems; controls and sensing products including valves, cylinders, electronic controls, electromechanical actuators, sensors, displays and panels, aircraft flap and slat systems and nose wheel steering systems; fluid conveyance products, including hose, thermoplastic tubing, fittings, adapters, couplings, sealing and ducting; and fuel systems including fuel pumps, sensors, valves, adapters and regulators. The principal markets for the Aerospace segment are manufacturers of commercial and military aircraft and related after-market customers. These manufacturers and other customers operate globally, and these products are sold and serviced through a variety of channels.

Truck

The Truck segment is a leader in the design, manufacture and marketing of a complete line of drivetrain and powertrain systems and components for performance, fuel economy and safety for commercial vehicles. Products include transmissions, clutches and hybrid power systems. The principal markets for the Truck segment are original equipment manufacturers and after-market customers of heavy, medium and light-duty trucks and passenger cars. These manufacturers and other customers are located globally, and most sales of these products are made directly to these customers.

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Automotive

The Automotive segment is a leading supplier of automotive drivetrain and powertrain systems for performance, fuel economy and safety including critical components that reduce emissions and fuel consumption and improve stability, performance, fuel economy and safety of cars, light trucks and commercial vehicles. Products include superchargers, engine valves and valve actuation systems, cylinder heads, locking and limited slip differentials, transmission and engine controls, fuel vapor components, compressor control clutches for mobile refrigeration, fluid connectors and hoses for air conditioning and power steering, underhood plastic components, fluid conveyance products including, hose, thermoplastic tubing, fittings, adapters, couplings and sealing products to the global automotive industry. The principal markets for the Automotive segment are original equipment manufacturers and aftermarket customers of light-duty trucks, SUVs, CUVs, and passenger cars. These manufacturers and other customers are located globally, and most sales of these products are made directly to these customers.

Our principal executive office is located at Eaton Center, 1111 Superior Avenue, Cleveland, Ohio 44114-2584, and our telephone number is (216) 523-5000.

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Except as may be described otherwise in a prospectus supplement or term sheet, we will use the net proceeds from the sale of the securities under this prospectus for general corporate purposes, which may include additions to working capital, acquisitions, or the retirement of existing indebtedness via repayment, redemption or exchange.

RATIO OF EARNINGS TO FIXED CHARGES

The following table shows our ratio of earnings to fixed charges for each of the five years in the period ended December 31, 2011.

	For the Years Ended December 31,				
	2011	2010	2009	2008	2007
Ratio of Earnings to Fixed Charges	7.81	5.50	2.29	5.26	5.16

For the purpose of computing the ratio of earnings to fixed charges, earnings consist of consolidated pretax income from continuing operations before adjustment for minority interests in consolidated subsidiaries and income (loss) of equity investees, plus (1) amortization of capitalized interest, (2) distributed income of equity investees and (3) fixed charges described below, excluding interest capitalized. Fixed charges consist of (1) interest expensed, (2) capitalized interest, (3) amortization of debt issue costs and (4) that portion of rent expense estimated to represent interest. Because we have not had any preferred shares outstanding during the last five years and have, therefore, not paid any dividends on preferred shares, our ratio of earnings to combined fixed charges and preferred share dividends has been the same as the ratio of earnings to fixed charges for each of the above periods.

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DESCRIPTION OF DEBT SECURITIES

We may issue debt securities from time to time in one or more distinct series. This section summarizes the material terms of the debt securities that are common to all series. Most of the financial terms and other specific material terms of any series of debt securities that we offer will be described in a prospectus supplement or term sheet. Furthermore, since the terms of specific debt securities may differ from the general information we have provided below, you should rely on information in the prospectus supplement or term sheet that is inconsistent with the information below. As used in this section, we, us, our and our company refer to Eaton Corporation and not to its subsidiaries, unless the context otherwise requires.

The debt securities are governed by a document called an indenture. An indenture is a contract between us and a financial institution acting as Trustee on your behalf. The Trustee has two main roles. First, the Trustee can enforce your rights against us if we default. There are some limitations on the extent to which the Trustee acts on your behalf. Second, the Trustee performs certain administrative duties for us.

The debt securities will be issued under an indenture dated as of April 1, 1994, (as may be supplemented from time to time the Indenture), between us and The Bank of New York Mellon Trust Company N.A., as successor to JPMorgan Chase Bank, N.A. (formerly known as Chemical Bank), as trustee (the Trustee). The Indenture is subject to and governed by the Trust Indenture Act of 1939, as amended (the Trust Indenture Act).

The Indenture and associated documents contain the full legal text of the matters described in this section. The Indenture is filed as an exhibit to the registration statement to which this prospectus is a part.

Because this section is a summary of the material terms of the Indenture, it does not describe every aspect of the debt securities. This summary is qualified in its entirety by the provisions of the Indenture, including definitions of certain terms used in the Indenture. For example, in this section, we use capitalized words to signify terms that are specifically defined in the Indenture. Some of the definitions are repeated in this prospectus, but for the rest you will need to read the Indenture. We also include references in parentheses to certain sections of the Indenture or the Trust Indenture Act. Whenever we refer to particular sections or defined terms of the Indenture, those sections or defined terms are incorporated by reference in this prospectus or in the prospectus supplement or term sheet. Unless otherwise noted, the section numbers refer to the applicable section of the Indenture.

General

The debt securities will be our unsecured obligations and will rank equally with all of our other unsecured and unsubordinated indebtedness.

Under the Indenture, we may issue any debt securities offered under this prospectus and the accompanying prospectus supplement or term sheet (offered debt securities) and any debt securities issuable upon the exercise of debt warrants or upon conversion or exchange of other offered securities (underlying debt securities), as well as other unsecured debt securities.

With respect to the offered debt securities and any underlying debt securities, you should read the prospectus supplement or term sheet for the following terms and other material terms, which will be established by authority of our Board of Directors or pursuant to an officers' certificate or a supplement to the Indenture before the issuance of the debt securities:

the title of the debt securities and whether the securities are convertible securities;

the total principal amount of the debt securities and any limit on the total principal amount of debt securities of each series;

the date or dates when the principal of the debt securities will be payable or how those dates will be determined or extended;

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the interest rate or rates, which may be fixed or variable, that the debt securities will bear, if any, or how such rate or rates will be determined, the date or dates from which any interest will accrue, if any, or how such date or dates will be determined, the interest payment dates, the record dates for such payments, if any, or how such date or dates will be determined and the basis upon which interest will be calculated, if other than that of a 360-day year or twelve 30-day months;

whether the amount of payments of principal of (or premium, if any), or interest on, the debt securities will be determined with reference to an index, formula or other method (which could be based on one or more Currencies, commodities, equity indices or other indices) and how such amounts will be determined;

any optional redemption provisions;

any sinking fund or other provisions that would obligate us to repurchase or otherwise redeem the debt securities;

if other than U.S. dollars, the Currency or Currencies of the debt securities;

if other than denominations of \$1,000 in the case of Registered Securities, the denominations in which the offered debt securities will be issued;

if not the principal amount of the debt securities, the portion of the principal amount at which the debt securities will be issued and, if not the principal amount of the debt securities, the portion of the principal amount payable upon acceleration of the maturity of the debt securities or how that portion will be determined;

the form of the debt securities, if other than a registered global note, including whether the debt securities are to be issuable in permanent or temporary global form, as Registered Securities, Bearer Securities or both, any restrictions on the offer, sale or delivery of Bearer Securities, and the terms, if any, upon which you may exchange Bearer Securities for Registered Securities and vice versa (if permitted by applicable laws and regulations);

any modifications or additions to the provisions of Article Fourteen of the Indenture described below under **Defeasance and Covenant Defeasance** if that Article is applicable to the debt securities;

any changes or additions to the Events of Default or our covenants with respect to the debt securities;

the place or places, if any, other than or in addition to The City of New York, of payment, transfer, conversion and/or exchange of the debt securities, and where notices or demands to or upon us in respect of the debt securities may be served;

whether we or a holder may elect payment of the principal or interest in one or more Currencies other than that in which such debt securities are stated to be payable, and the period or periods within which, and the terms and conditions upon which, that election may be made, and the time and manner of determining the exchange rate between the Currency or Currencies in which they are stated to be payable and the Currency or Currencies in which they are to be so payable;

if other than the Trustee, the identity of each Security Registrar and/or Paying Agent;

the designation of the Exchange Rate Agent, if applicable;

the Person to whom any interest on any Registered Security of the series will be payable, if other than the registered holder at the close of business on the record date, the manner in which, or the Person to whom, any interest on any Bearer Security of the series will be payable, if not upon presentation and surrender of the coupons relating to the Bearer Security as they mature, and the extent to which, or the manner in which, any interest payable on a temporary global security on an Interest Payment Date will be paid if not in the manner provided in the Indenture;

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whether and under what circumstances we will pay additional amounts as contemplated by Section 1005 of the Indenture (Additional Amounts) in respect of any tax, assessment or governmental charge and, if so, whether we will have the option to redeem the debt securities rather than pay the Additional Amounts (and the terms of any such option);

any provisions granting special rights to the holders of the debt securities upon the occurrence of specified events;

in the case of convertible securities, any terms by which they may be convertible into common shares;

if we issue the debt securities in definitive form, the terms and conditions under which definitive securities will be issued;

if we issue the debt securities upon the exercise of warrants, the time, manner and place for them to be authenticated and delivered;

the manner for paying principal and interest and the manner for transferring the debt securities; and

any other terms of the debt securities that are consistent with the requirements of the Trust Indenture Act.

For purposes of this prospectus, any reference to the payment of principal of (or premium, if any) or interest on debt securities will include Additional Amounts if required by the terms of the debt securities.

The Indenture does not limit the amount of debt securities that we are authorized to issue from time to time. (Section 301) When a single Trustee is acting for all debt securities issued under the Indenture, those Securities are called the Indenture Securities. The Indenture also provides that there may be more than one Trustee thereunder, each for a series of Indenture Securities. At a time when two or more Trustees are acting under the Indenture, each with respect to only certain series, the term Indenture Securities means the series of debt securities for which each respective Trustee is acting. If there is more than one Trustee under the Indenture, the powers and trust obligations of each Trustee will apply only to the Indenture Securities for which it is Trustee. If two or more Trustees are acting under the Indenture, then the Indenture Securities for which each Trustee is acting would be treated as if issued under separate indentures.

The Indenture does not contain any provisions that give you protection in the event we issue a large amount of debt or we are acquired by another entity.

We may issue Indenture Securities with terms different from those of Indenture Securities already issued. Without the consent of the holders thereof, we may reopen a previous issue of a series of Indenture Securities and issue additional Indenture Securities of that series unless the reopening was restricted when that series was created.

There is no requirement that we issue debt securities in the future under the Indenture, and we may use other indentures or documentation containing different provisions in connection with future issues of such other debt securities.

We may issue the debt securities as original issue discount securities , which are debt securities, including any zero-coupon debt securities, that are issued and sold at a discount from their stated principal amount. Original issue discount securities provide that, upon acceleration of their maturity, an amount less than their principal amount will become due and payable. We will describe United States federal income tax consequences and other considerations applicable to original issue discount securities in any prospectus supplement or term sheet relating to them.

Unless otherwise specified in the applicable prospectus supplement or term sheet, the debt securities will be denominated in U.S. dollars and all payments on the debt securities will be made in U.S. dollars. If any series of debt securities is sold for, payable in or denominated in one or more foreign Currencies, we will specify applicable restrictions, elections, tax consequences, specific terms and other information in the applicable prospectus supplement or term sheet. For further information regarding foreign currency debt securities, see Foreign Currency Risk Fluctuations and Controls below.

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Payment of the purchase price of the debt securities must be made in immediately available funds.

As used in this prospectus, **Business Day** means any day, other than a Saturday or Sunday, that is neither a legal holiday nor a day on which commercial banks are authorized or required by law, regulation or executive order to close in The City of New York; *provided, however*, that, with respect to foreign currency debt securities, the day is also not a day on which commercial banks are authorized or required by law, regulation or executive order to close in the Principal Financial Center (as defined below) of the country issuing the specified currency (or, if the specified currency is the euro, the day is also a day on which the Trans-European Automated Real-Time Gross Settlement Express Transfer (TARGET) System is open); and *provided further* that, with respect to debt securities as to which LIBOR is an applicable interest rate basis, the day is also a London Business Day.

London Business Day means a day on which commercial banks are open for business (including dealings in the designated LIBOR Currency) in London.

Principal Financial Center means (i) the capital city of the country issuing the specified currency or (ii) the capital city of the country to which the designated LIBOR Currency relates, as applicable, except that the term **Principal Financial Center** means the following cities in the case of the following currencies:

Currency	Principal Financial Center
U.S. dollars	The City of New York
Australian dollars	Sydney
Canadian dollars	Toronto
New Zealand dollars	Auckland
South African rand	Johannesburg
Swiss francs	Zurich

and in the event the LIBOR Currency is euro, the **Principal Financial Center** is London.

LIBOR Currency means the currency specified in the applicable prospectus supplement or term sheet as to which LIBOR shall be calculated or, if no such currency is specified in the applicable prospectus supplement or term sheet, U.S. dollars.

The authorized denominations of debt securities denominated in U.S. dollars will be integral multiples of \$1,000. The authorized denominations of foreign currency debt securities will be set forth in the applicable prospectus supplement or term sheet.

Optional Redemption, Repayment and Repurchase

The prospectus supplement or term sheet for a debt security will indicate whether we will have the option to redeem the debt security before the stated maturity and the price and date or dates on which redemption may occur. If we are allowed to redeem a debt security, we may exercise the option by notifying the Trustee and the paying agent at least 45 days prior to the redemption date. In the case we elect to redeem less than all of a series of debt securities, we may exercise the option by notifying the Trustee and the paying agent at least 60 days prior to the redemption date. At least 30 but not more than 60 days before the redemption date, the Trustee will mail notice or cause the paying agent to mail notice of redemption to the holders. If a debt security is only redeemed in part, we will issue a new debt security or debt securities for the unredeemed portion.

The prospectus supplement or term sheet relating to a debt security will also indicate whether you will have the option to elect repayment by us prior to the stated maturity and the price and the date or dates on which repayment may occur.

For a debt security to be repaid at your election, the paying agent must receive, at least 30 but not more than 45 days prior to an optional repayment date, if, in certificated form, such debt security with the form entitled **Option to Elect Repayment** on the reverse of the debt security duly completed. You may also send the paying agent a facsimile or letter from a member of a national securities exchange or the Financial Industry Regulatory Authority (**FINRA**) or a commercial bank or trust company in the United States describing the particulars of the repayment, including a guarantee that the debt security and the form entitled **Option to Elect Repayment** will be

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received by the paying agent no later than five Business Days after such facsimile or letter. If you present a debt security for repayment, such act will be irrevocable. You may exercise the repayment option for less than the entire principal of the debt security, *provided* the remaining principal outstanding is an authorized denomination. If you elect partial repayment, your debt security will be cancelled, and we will issue a new debt security or debt securities for the remaining amount.

The Depository Trust Company or its nominee will be the holder of each global security and will be the only party that can exercise a right of repayment. If you are a beneficial owner of a global security and you want to exercise your right of repayment, you must instruct your broker or indirect participant through which you hold your interest to notify The Depository Trust Company. You should consult your broker or such indirect participant to discuss the appropriate cut-off times and any other requirements for giving this instruction. The giving of any such instruction will be irrevocable.

Regardless of anything in this prospectus, if a debt security is an OID Note (as defined below) (other than an Indexed Note), the amount payable in the event of redemption or repayment prior to its stated maturity will be the amortized face amount on the redemption or repayment date, as the case may be. The amortized face amount of an OID Note will be equal to (i) the issue price specified in the applicable prospectus supplement or term sheet plus (ii) that portion of the difference between the issue price and the principal amount of the debt security that has accrued at the yield to maturity described in the prospectus supplement or term sheet (computed in accordance with generally accepted U.S. bond yield computation principles) by the redemption or repayment date. However, in no case will the amortized face amount of an OID Note exceed its principal amount.

Regardless of anything in this prospectus, if a debt security is an OID Note (as defined below) (other than an Indexed Note), the amount payable in the event of acceleration shall be the portion of principal amount specified in the terms of that series of notes to be due and payable immediately.

We may at any time purchase debt securities at any price in the open market or otherwise. We may hold, resell or surrender for cancellation any debt securities that we purchase.

Conversion and Exchange

If you may convert or exchange debt securities for other Securities, the prospectus supplement or term sheet will explain the terms and conditions of such conversion or exchange, including:

the conversion price or exchange ratio (or the calculation method);

the conversion or exchange period (or how such period will be determined);

if conversion or exchange will be mandatory, at your option or at our option;

provisions for adjustment of the conversion price or the exchange ratio; and

provisions affecting conversion or exchange in the event of the redemption of the debt securities.

The terms may also include provisions under which the number or amount of other Securities to be received by the holders of such debt securities upon conversion or exchange would be calculated according to the market price of such other Securities as of a time stated in the prospectus supplement or term sheet.

Issuance of Securities in Registered Form

We may issue the debt securities in registered form, in which case we will issue them in book-entry form only. Debt securities issued in book-entry form will be represented by global securities. The prospectus supplement or term sheet will also describe the requirements with

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respect to our maintenance of offices or agencies outside the United States and the applicable U.S. federal tax law requirements.

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Book-Entry Holders. We will issue registered debt securities in book-entry form only, unless we specify otherwise in the applicable prospectus supplement or term sheet. This means debt securities will be represented by one or more global securities registered in the name of a depository. Financial institutions that participate in the depository's book-entry system will hold beneficial interests in the debt securities held by or on behalf of the depository or its nominee. These institutions may hold these interests on behalf of themselves or customers.

Under the Indenture, only the person in whose name a debt security is registered is recognized as the holder of that debt security. Consequently, for debt securities issued in book-entry form, we will recognize only the depository or its nominee as the holder of the debt securities and we will make all payments on the debt securities to the depository. The depository will then pass along the payments it receives to its participants, which, in turn, will pass the payments along to their customers who are the beneficial owners. The depository and its participants will do so under agreements they have made with one another or with their customers; they are not obligated to do so under the terms of the debt securities or the indenture.

As a result, investors will not own debt securities directly. Instead, they will own beneficial interests in a global security, through a bank, broker or other financial institution that participates in the depository's book-entry system or holds an interest through an indirect participant. As long as the debt securities are represented by one or more global securities, investors will be indirect holders, and not holders of the debt securities.

Legal Holders. Our obligations, as well as the obligations of the trustee and those of any third parties employed by us or the trustee, run only to the legal holders of the debt securities. We do not have obligations to investors who hold beneficial interests in global securities, in street name or by any other indirect means. This will be the case whether an investor chooses to be an indirect holder of a debt security or has no choice because we are issuing the debt securities only in book-entry form.

For example, once we make a payment or give a notice to the holder, we have no further responsibility for the payment or notice even if that holder is required, under agreements with depository participants or customers or by law, to pass it along to the indirect holders but does not do so. Similarly, if we want to obtain the approval of the holders for any purpose (for example, to amend the Indenture or to relieve us of the consequences of a default or of our obligation to comply with a particular provision of the Indenture), we would seek the approval only from the holders, and not the indirect holders, of the debt securities. Whether and how the holders contact the indirect holders is up to the holders.

When we refer to you, we mean those who invest in the debt securities being offered by this prospectus, the prospectus supplement or term sheet whether they are the holders or only indirect holders of those debt securities. When we refer to your debt securities, we mean the debt securities in which you hold a direct or indirect interest.

Special Considerations for Indirect Holders. If you hold debt securities through a bank, broker or other financial institution, either in book-entry form or in street name, we urge you to check with that institution to find out:

how it handles securities payments and notices,

whether it imposes fees or charges,

how it would handle a request for the holders' consent, if ever required,

whether and how you can instruct it to send you debt securities registered in your own name so you can be a holder, if that is permitted in the future for a particular series of debt securities,

how it would exercise rights under the debt securities if there were a default or other event triggering the need for holders to act to protect their interests, and

if the debt securities are in book-entry form, how the depository's rules and procedures will affect these matters.

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Interest and Interest Rates

General

Each debt security will begin to accrue interest from the date it is originally issued. The related prospectus supplement or term sheet will specify each debt security as a Fixed Rate Note, a Floating Rate Note, an Amortizing Note or an Indexed Note and describe the method of determining the interest rate, including any spread and/or spread multiplier. For an Indexed Note, the related prospectus supplement or term sheet also will describe the method for the calculation and payment of principal and interest. The prospectus supplement or term sheet for a Floating Rate Note or Indexed Note may also specify a maximum and a minimum interest rate.

A debt security may be issued as a Fixed Rate Note or a Floating Rate Note or as a debt security that combines fixed and floating rate terms.

Interest rates offered with respect to debt securities may differ depending upon, among other things, the aggregate principal amount of debt securities purchased in any single transaction. Debt securities with similar variable terms but different interest rates, as well as debt securities with different variable terms, may be offered concurrently to different investors. Interest rates or formulas and other terms of debt securities are subject to change from time to time, but no such change will affect any debt security already issued or as to which an offer to purchase has been accepted.

Interest on the debt securities denominated in U.S. dollars will be paid by check mailed on an Interest Payment Date other than a Maturity Date (as defined below) to the persons entitled thereto to the addresses of such holders as they appear in the security register or, at our option, by wire transfer to a bank account maintained by the holder. The principal of, premium, if any, and interest on debt securities denominated in U.S. dollars, together with interest accrued and unpaid thereon, due on the Maturity Date will be paid in immediately available funds upon surrender of such debt securities at the corporate trust office of the Trustee in The City of New York, or, at our option, by wire transfer of immediately available funds to an account with a bank designated at least 15 calendar days prior to the Maturity Date by the applicable registered holder, *provided* the particular bank has appropriate facilities to receive these payments and the particular debt security is presented and surrendered at the office or agency maintained by us for this purpose in the Borough of Manhattan, The City of New York, in time for the Trustee to make these payments in accordance with its normal procedures.

Fixed Rate Notes

The prospectus supplement or term sheet for debt securities with a fixed interest rate (Fixed Rate Notes) will describe a fixed interest rate payable semiannually in arrears on dates specified in such prospectus supplement or term sheet (each, with respect to Fixed Rate Notes, an Interest Payment Date). Unless otherwise specified in a prospectus supplement or term sheet, interest on Fixed Rate Notes will be computed on the basis of a 360-day year of twelve 30-day months. If the stated maturity date, any redemption date or any repayment date (together referred to as the Maturity Date) or an Interest Payment Date for any Fixed Rate Note is not a Business Day, principal of, premium, if any, and interest on that debt security will be paid on the next Business Day, and no interest will accrue from and after the Maturity Date or Interest Payment Date. Interest on Fixed Rate Notes will be paid to holders of record as of each Regular Record Date as determined in the applicable prospectus supplement or term sheet.

Each interest payment on a Fixed Rate Note will include interest accrued from, and including, the issue date or the last Interest Payment Date to which interest has been paid or duly provided for, as the case may be, to but excluding the applicable Interest Payment Date or the Maturity Date, as the case may be.

Original Issue Discount Notes

We may issue original issue discount debt securities (including zero coupon debt securities) (OID Notes), which are debt securities issued at a discount from the principal amount payable on the Maturity Date. There may not be any periodic interest payments on OID Notes. For OID Notes, interest normally accrues during the life of the debt security and is paid on the Maturity Date. Upon a redemption, repayment or acceleration of the maturity of an OID Note, the amount payable will be determined as set forth under Optional Redemption, Repayment and Repurchase . This amount normally is less than the amount payable on the stated maturity date.

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Amortizing Notes

We may issue amortizing debt securities, which are Fixed Rate Notes for which combined principal and interest payments are made in installments over the life of each debt security (Amortizing Notes). Payments on Amortizing Notes are applied first to interest due and then to the reduction of the unpaid principal amount. The related prospectus supplement or term sheet for an Amortizing Note will include a table setting forth repayment information.

Floating Rate Notes

Each debt security with a floating interest rate (a Floating Rate Note) will have an interest rate basis or formula. That basis or formula may be based on:

the CD Rate;

the Commercial Paper Rate;

LIBOR;

the Federal Funds Rate;

the Prime Rate;

the Treasury Rate;

the CMT Rate;

the Eleventh District Cost of Funds Rate; or

another negotiated interest rate basis or formula.

The prospectus supplement or term sheet will also indicate any spread and/or spread multiplier.

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Regulatory and other long-term assets:

Regulatory assets

1,298

1,289

Goodwill

1,345

1,345

Other

72

72

Total regulatory and other long-term assets

2,715

2,706

TOTAL ASSETS

\$

18,610

\$

18,482

The accompanying notes are an integral part of these consolidated financial statements.

3

American Water Works Company, Inc. and Subsidiary Companies

Consolidated Balance Sheets (Unaudited)

(In millions, except share and per share data)

	March 31, 2017	December 31, 2016
CAPITALIZATION AND LIABILITIES		
Capitalization:		
Common stock (\$0.01 par value, 500,000,000 shares authorized, 182,231,713 and 181,798,555 shares issued, respectively)	\$ 2	\$ 2
Paid-in-capital	6,400	6,388
Accumulated deficit	(759)	(873)
Accumulated other comprehensive loss	(82)	(86)
Treasury stock, at cost (4,502,221 and 3,701,867 shares, respectively)	(274)	(213)
Total common stockholders' equity	5,287	5,218
Long-term debt	5,744	5,749
Redeemable preferred stock at redemption value	9	10
Total long-term debt	5,753	5,759
Total capitalization	11,040	10,977
Current liabilities:		
Short-term debt	980	849
Current portion of long-term debt	574	574
Accounts payable	108	154
Accrued liabilities	453	609
Taxes accrued	67	31
Interest accrued	101	63
Other	135	112
Total current liabilities	2,418	2,392
Regulatory and other long-term liabilities:		
Advances for construction	297	300
Deferred income taxes, net	2,629	2,596
Deferred investment tax credits	23	23
Regulatory liabilities	404	403
Accrued pension expense	420	419
Accrued postretirement benefit expense	86	87
Other	68	67
Total regulatory and other long-term liabilities	3,927	3,895
Contributions in aid of construction	1,225	1,218
Commitments and contingencies (see Note 8)		
TOTAL CAPITALIZATION AND LIABILITIES	\$ 18,610	\$ 18,482

The accompanying notes are an integral part of these consolidated financial statements.

American Water Works Company, Inc. and Subsidiary Companies

Consolidated Statements of Operations (Unaudited)

(In millions, except per share data)

	For the Three Months Ended March 31,	
	2017	2016
Operating revenues	\$756	\$743
Operating expenses:		
Operation and maintenance	337	348
Depreciation and amortization	124	116
General taxes	68	66
Gain on asset dispositions and purchases	-	(1)
Total operating expenses, net	529	529
Operating income	227	214
Other income (expense):		
Interest, net	(85)	(80)
Other, net	3	2
Total other income (expense)	(82)	(78)
Income from continuing operations before income taxes	145	136
Provision for income taxes	52	54
Net income attributable to common stockholders	\$93	\$82
Basic earnings per share:		
Net income attributable to common stockholders	\$0.52	\$0.46
Diluted earnings per share:		
Net income attributable to common stockholders	\$0.52	\$0.46
Weighted-average common shares outstanding:		
Basic	178	178
Diluted	179	179
Dividends declared per common share	—	—

The accompanying notes are an integral part of these consolidated financial statements.

American Water Works Company, Inc. and Subsidiary Companies

Consolidated Statements of Comprehensive Income (Unaudited)

(In millions)

	For the Three Months Ended March 31,	
	2017	2016
Net income attributable to common stockholders	\$93	\$82
Other comprehensive income (loss), net of tax:		
Pension amortized to periodic benefit cost:		
Actuarial loss, net of tax of \$1 in 2017 and 2016	2	1
Foreign currency translation adjustment	(1)	1
Unrealized gain (loss) on cash flow hedges, net of tax of \$2 and \$(1) in 2017 and 2016, respectively	3	(1)
Net other comprehensive income	4	1
Comprehensive income attributable to common stockholders	\$97	\$83

The accompanying notes are an integral part of these consolidated financial statements.

American Water Works Company, Inc. and Subsidiary Companies

Consolidated Statements of Cash Flows (Unaudited)

(In millions)

	For the Three Months Ended March 31,	
	2017	2016
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	\$93	\$82
Adjustments to reconcile to net cash flows provided by operating activities:		
Depreciation and amortization	124	116
Deferred income taxes and amortization of investment tax credits	64	65
Provision for losses on accounts receivable	4	6
Gain on asset dispositions and purchases	—	(1)
Pension and non-pension postretirement benefits	15	15
Other non-cash, net	(18)	(24)
Changes in assets and liabilities:		
Receivables and unbilled revenues	51	49
Pension and non-pension postretirement benefit contributions	(11)	(14)
Accounts payable and accrued liabilities	(72)	15
Other assets and liabilities, net	27	(49)
Net cash provided by operating activities	277	260
CASH FLOWS FROM INVESTING ACTIVITIES		
Capital expenditures	(270)	(284)
Acquisitions	(2)	(22)
Proceeds from sale of assets and securities	—	1
Removal costs from property, plant and equipment retirements, net	(13)	(17)
Net funds restricted	(3)	(1)
Net cash used in investing activities	(288)	(323)
CASH FLOWS FROM FINANCING ACTIVITIES		
Repayments of long-term debt	(4)	(11)
Net short-term borrowings with maturities less than three months	131	211
Proceeds from issuances of employee stock plans and DRIP	10	10
Advances and contributions for construction, net of refunds of \$4 and		
\$4, respectively	7	7
Debt issuance costs	—	(1)
Dividends paid	(67)	(61)
Anti-dilutive stock repurchase	(54)	(62)
Taxes paid related to employee stock plans	(9)	(9)
Net cash provided by financing activities	14	84
Net increase in cash and cash equivalents	3	21
Cash and cash equivalents as of beginning of period	75	45

Cash and cash equivalents as of end of period	\$78	\$66
Non-cash investing activity:		
Capital expenditures acquired on account but unpaid as of end of period	\$142	\$166

The accompanying notes are an integral part of these consolidated financial statements.

American Water Works Company, Inc. and Subsidiary Companies

Consolidated Statements of Changes in Stockholders' Equity (Unaudited)

(In millions)

	Common Stock	Par Value	Paid-in-Capital	Accumulated Deficit	Accumulated Other Comprehensive Loss	Treasury Stock At Cost	Total Stockholders' Equity	
	Shares					Shares		
Balance as of December 31, 2016	181.8	\$ 2	\$ 6,388	\$ (873)	\$ (86)	(3.7)	\$ (213)	\$ 5,218
Cumulative effect of change in								
accounting principle	—	—	—	21	—	—	—	21
Net income attributable to common stockholders	—	—	—	93	—	—	—	93
Direct stock reinvestment and								
purchase plan	—	—	3	—	—	—	—	3
Employee stock purchase plan	—	—	2	—	—	—	—	2
Stock-based compensation activity	0.4	—	7	—	—	(0.1)	(7)	-
Repurchases of common stock	—	—	—	—	—	(0.7)	(54)	(54)
Net other comprehensive income								
(loss)	—	—	—	—	4	—	—	4
Balance as of March 31, 2017	182.2	\$ 2	\$ 6,400	\$ (759)	\$ (82)	(4.5)	\$ (274)	\$ 5,287

	Common Stock	Par Value	Paid-in-Capital	Accumulated Deficit	Accumulated Other Comprehensive Loss	Treasury Stock At Cost	Total Stockholders' Equity	
	Shares					Shares		
Balance as of December 31, 2015	180.9	\$ 2	\$ 6,351	\$ (1,073)	\$ (88)	(2.6)	\$ (143)	\$ 5,049
Net income attributable to common stockholders	—	—	—	82	—	—	—	82
Direct stock reinvestment and	—	—	1	—	—	—	—	1

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purchase plan								
Employee stock purchase plan	—	—	1	—	—	—	—	1
Stock-based compensation activity	0.5	—	15	—	—	(0.1)	(5)	10
Repurchases of common stock	—	—	—	—	—	(1.0)	(62)	(62)
Net other comprehensive income								
(loss)	—	—	—	—	1	—	—	1
Balance as of March 31, 2016	181.4	\$ 2	\$ 6,368	\$ (991)\$ (87) (3.7)	\$(210)	\$ 5,082

The accompanying notes are an integral part of these consolidated financial statements.

American Water Works Company, Inc. and Subsidiary Companies

Notes to Consolidated Financial Statements (Unaudited)

(Unless otherwise noted, in millions, except per share data)

Note 1: Basis of Presentation

The unaudited consolidated financial statements provided in this report include the accounts of American Water Works Company, Inc. and all of its subsidiaries (collectively, “American Water” or the “Company”) in which a controlling interest is maintained after the elimination of intercompany accounts and transactions. The financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”) for interim financial reporting and with the rules and regulations for reporting on Form 10-Q. Accordingly, they do not contain certain information and disclosures required by GAAP for comprehensive financial statements. In the opinion of management, all adjustments necessary for a fair statement of the financial position as of March 31, 2017 and results of operations and cash flows for all periods presented have been made. All adjustments are of a normal, recurring nature, except as otherwise disclosed.

The Consolidated Balance Sheet as of December 31, 2016 is derived from the Company's audited consolidated financial statements as of December 31, 2016. The unaudited financial statements and notes included in this report should be read in conjunction with the Company's Annual Report on Form 10-K for the year ended December 31, 2016 (“Form 10-K”) which provides a more complete discussion of the Company's accounting policies, financial position, operating results and other matters. The results of operations for interim periods are not necessarily indicative of the results that may be expected for the year, due primarily to the seasonality of the Company's operations.

Note 2: New Accounting Standards

The Company adopted the following accounting standard on January 1, 2017:

Standard	Description	Date of Adoption	Application	Effect on the Consolidated Financial Statements (or Other Significant Matters)
Simplification of Employee Share-Based Payment Accounting	Simplified accounting and disclosure requirements for share-based payment awards. The updated guidance addresses simplification in areas such as: (i) the recognition of excess tax benefits and	January 1, 2017	Modified retrospective for the recognition of excess tax benefits and deficiencies; full retrospective for the classification of excess tax benefits and taxes	The adoption of this standard resulted in a cumulative effect to increase retained earnings by \$21, with an offsetting decrease to deferred income taxes, net. Also, the adoption resulted in a net increase in cash flows from operating activities and a net decrease in cash flows from financing activities of \$14 and \$13 for the three months ended March 31, 2017 and 2016, respectively, on the Consolidated Statements

deficiencies; (ii) the classification of excess tax benefits and taxes paid on the Consolidated Statements of Cash Flows; (iii) election of an accounting policy for forfeitures; and (iv) the amount an employer can withhold to cover income taxes and still qualify for equity classification.

paid on the Consolidated Statements of Cash Flows

of Cash Flows.

The following recently issued accounting standards are not yet required to be adopted by the Company as of March 31, 2017:

Standard	Description	Date of Adoption	Application	Effect on the Consolidated Financial Statements (or Other Significant Matters)
Revenue from Contracts with Customers	Changes the criteria for recognizing revenue from a contract with a customer. Replaces existing guidance on revenue recognition, including most industry specific guidance. The objective is to provide a single, comprehensive revenue recognition model for all contracts with customers to improve comparability within industries, across industries and across capital markets. The underlying principle is that an entity will recognize revenue to depict the transfer of goods and services to customers at an amount the entity expects to be entitled to in exchange for those goods or services. The guidance also requires a number of disclosures regarding the nature, amount, timing and uncertainty of revenue and related cash flows.	January 1, 2018; early adoption permitted	Full or modified retrospective	The Company is evaluating the impact on the consolidated financial statements and related disclosures, as well as the transition method to be used to adopt the guidance. The Company is also considering the impacts of the new standard on its accounting for contributions in aid of construction. The Company does not expect to early adopt.
Classification of Certain Cash Receipts and Cash Payments on the Statement of Cash Flows	Provides guidance on the presentation and classification in the statement of cash flows for the following cash receipts and payments: (i) debt prepayment or debt extinguishment costs; (ii) settlement of zero-coupon debt instruments or other debt instruments with coupon interest rates that are insignificant in relation to the effective interest rate of the	January 1, 2018; early adoption permitted	Retrospective	The Company does not anticipate significant impacts on its Consolidated Statements of Cash Flows.

borrowing; (iii) contingent consideration payments made after a business combination; (iv) proceeds from the settlement of insurance claims; (v) proceeds from the settlement of corporate-owned life insurance policies, including bank-owned life insurance policies; (vi) distributions received from equity method investees; (vii) beneficial interests in securitization transactions; and (viii) separately identifiable cash flows and application of the predominance principle.

Presentation of Changes in Restricted Cash on the Statement of Cash Flows	Updates the accounting and disclosure guidance for the classification and presentation of changes in restricted cash on the statements of cash flows. The amended guidance requires that the statements of cash flows explain the change during the period in the total of cash, cash equivalents and amounts described as restricted cash or restricted cash equivalents. Restricted cash and restricted cash equivalents will now be included with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts shown on the statements of cash flows.	January 1, 2018; early adoption permitted	Retrospective	The Company does not anticipate significant impacts on its Consolidated Statements of Cash Flows.
Clarifying the Definition of a Business	Updates the accounting guidance to clarify the definition of a business with the objective of assisting entities with evaluating whether transactions should be accounted for as acquisitions, or disposals, of assets or businesses.	January 1, 2018; early adoption permitted	Prospective	The Company is evaluating the impact on the consolidated financial statements and related disclosures.
Gains and Losses from the Derecognition of Nonfinancial	Updated the guidance to clarify the accounting for gains and losses resulting from the derecognition of nonfinancial	January 1, 2018; early adoption	Full or modified retrospective	The Company is evaluating the impact on the consolidated financial statements and related disclosures.

Assets	assets and partial sale of nonfinancial assets. The guidance also clarifies the definition of an in-substance nonfinancial asset.	permitted		
Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost	Updated authoritative guidance requires the service cost component of net periodic benefit cost to be presented in the same income statement line item(s) as other employee compensation costs arising from services rendered during the period. The remaining components of net periodic benefit cost are required to be presented separately from the service cost component in an income statement line item outside of operating income. Also, the guidance allows for only the service cost component to be eligible for capitalization. The updated guidance does not impact the accounting for net periodic benefit costs as regulatory assets or liabilities.	January 1, 2018; early adoption permitted	Retrospective for the presentation of service cost component; prospective for the capitalization of service cost component	The Company is evaluating the impact on the consolidated financial statements and related disclosures.
Accounting for Leases	Updated the accounting and disclosure guidance for leasing arrangements. Under this guidance, a lessee will be required to recognize the following for all leases, excluding short-term leases, at the commencement date: (i) a lease liability, which is a lessee's obligation to make lease payments arising from a lease, measured on a discounted basis; and (ii) a right-of-use asset, which is an asset that represents the lessee's right to use, or control the use of, a specified asset for the lease term. Under the guidance, lessor accounting is largely unchanged.	January 1, 2019; early adoption permitted	Modified retrospective	The Company is evaluating the effect on the consolidated financial statements, related disclosures, as well as the timing of adoption.

Simplification of Goodwill Impairment Testing	Updated authoritative guidance which simplifies the subsequent measurement of goodwill by eliminating Step 2 from the goodwill impairment test. Under the amendments in the update, an entity should perform its annual, or interim, goodwill impairment test by comparing the fair value of a reporting unit with its carrying amount. An impairment charge should be recognized for the amount by which the carrying value exceeds the reporting unit's fair value, however, the loss recognized should not exceed the total amount of goodwill allocated to that reporting unit. An entity still has the option to perform the qualitative assessment for a reporting unit to determine if the quantitative impairment test is necessary.	January 1, 2020; early adoption permitted	Prospective	The Company is evaluating the impact on the consolidated financial statements and related disclosures, as well as the timing of adoption.
Measurement of Credit Losses	Updated the accounting guidance on reporting credit losses for financial assets held at amortized cost basis and available-for-sale debt securities. Under this guidance, expected credit losses are required to be measured based on historical experience, current conditions and reasonable and supportable forecasts that affect the collectability of the reported amount of financial assets. Also, this guidance requires that credit losses on available-for-sale debt securities be presented as an allowance rather than as a direct write-down.	January 1, 2020; early adoption permitted	Modified retrospective	The Company is evaluating the impact on the consolidated financial statements and related disclosures, as well as the timing of adoption.

Note 3: Acquisitions

During the three months ended March 31, 2017, the Company closed on two water system acquisitions for a total aggregate purchase price under \$1. Also, our Regulated Business made a non-escrowed deposit of \$2 related to the acquisition of the McKeesport, Pennsylvania wastewater system which is expected to close in the fourth quarter of 2017.

On April 3, 2017, the Company acquired all of the outstanding capital stock of Shorelands Water Company, Inc. for total consideration of \$33, in the form of approximately 0.4 shares of the Company's common stock. Assets acquired, principally utility plant, totaled \$26. Liabilities assumed totaled \$19, including \$5 of contributions in aid of construction, and assumed debt of \$6. This acquisition will be recorded during the second quarter of 2017 and includes \$27 of goodwill, which will be reported in the Company's Regulated Businesses segment. The preliminary price allocation related to this acquisition will be finalized once the valuation of assets acquired has been completed, no later than one year after the acquisition date.

Note 4: Stockholders' Equity

Accumulated Other Comprehensive Loss

The following table presents changes in accumulated other comprehensive loss by component, net of tax, for the three months ended March 31, 2017 and 2016, respectively:

	Defined Benefit Plans				Accumulated	
	Funded Status	Amortization of Prior Service Credits	Amortization of Actuarial Loss	Foreign Currency Translation	Gain (Loss) on Cash Flow Hedges	Other Comprehensive Loss
Beginning balance as of December 31, 2016	\$ (147)	\$ 1	\$ 42	\$ 2	\$ 16	\$ (86)
Other comprehensive income (loss)						
before reclassifications	—	—	—	(1)	3	2
Amounts reclassified from accumulated						
other comprehensive loss	—	—	2	—	—	2
Net other comprehensive income (loss)	—	—	2	(1)	3	4
Ending balance as of March 31, 2017	\$ (147)	\$ 1	\$ 44	\$ 1	\$ 19	\$ (82)
Beginning balance as of December 31, 2015	\$ (126)	\$ 1	\$ 36	\$ 2	\$ (1)	\$ (88)
Other comprehensive income (loss)						
before reclassifications	—	—	—	1	(1)	—
Amounts reclassified from accumulated						
other comprehensive loss	—	—	1	—	—	1
Net other comprehensive income (loss)	—	—	1	1	(1)	1
Ending balance as of March 31, 2016	\$ (126)	\$ 1	\$ 37	\$ 3	\$ (2)	\$ (87)

The Company does not reclassify the amortization of defined benefit pension cost components from accumulated other comprehensive loss directly to net income in its entirety, as a portion of these costs have been capitalized as a regulatory asset. These accumulated other comprehensive income loss components are included in the computation of net periodic pension cost. See Note 7— Pension and Other Postretirement Benefits.

The amortization of the loss on cash flow hedges is reclassified to net income during the period incurred and is included in interest, net in the accompanying Consolidated Statements of Operations.

Anti-dilutive Stock Repurchase Program

During the three months ended March 31, 2017, the Company repurchased 0.7 shares of common stock in the open market at an aggregate cost of \$54 under the anti-dilutive stock repurchase program authorized by the Company's Board of Directors in 2015. As of March 31, 2017, there were 6.1 shares of common stock available for repurchase under the program.

Note 5: Long-Term Debt

The following long-term debt was retired through sinking fund provisions, optional redemptions or payment at maturity during the three months ended March 31, 2017:

Company	Type	Rate	Maturity	Amount
	Private activity bonds and government			
American Water Capital Corp. (a)	funded debt—fixed rate	1.79%-2.90%	2021-2031	\$ 1
	Private activity bonds and government			
Other American Water subsidiaries	funded debt—fixed rate	0.00%-5.38%	2017-2041	2
Other American Water subsidiaries	Mandatorily redeemable preferred stock	8.49%	2036	1
Total retirements and redemptions				\$ 4

(a) American Water Capital Corp., which is a wholly owned subsidiary of the Company, has a support agreement with the Company that, under certain circumstances, is the functional equivalent of a guarantee. This indebtedness is considered "debt" for purposes of this support agreement.

The Company has four forward starting swap agreements with an aggregate notional amount of \$300 to reduce interest rate exposure on debt expected to be issued in 2017. These forward starting swap agreements terminate in December 2017 and have an average fixed rate of 2.20%. On February 8, 2017, the Company entered into a forward starting swap agreement with a notional amount of \$100 to reduce interest rate exposure for a portion of the expected refinancing of the Company's 5.62% fixed-rate long-term debt maturing in December 2018. This forward starting swap agreement terminates in November 2018 and has an average fixed rate of 2.67%. The Company has designated these forward starting swap agreements as cash flow hedges and the initial fair value, in addition to any subsequent changes in fair value, are recognized in accumulated other comprehensive gain or loss. Upon termination, the cumulative gain or loss recorded in accumulated other comprehensive gain or loss will be amortized through interest, net over the term of the issued debt.

The Company has an interest rate swap to hedge \$100 of its 6.085% fixed-rate debt maturing in 2017. The Company pays variable interest of six-month LIBOR plus 3.422% and the interest rate swap matures with the fixed-rate debt in

2017. The Company has designated the interest rate swap as a fair value hedge accounted for at fair value with gains or losses, as well as the offsetting gains or losses on the hedged item, recognized in interest, net. The net gain recognized by the Company was de minimis for the three months ended March 31, 2017 and 2016.

The Company has employed interest rate swaps to fix the interest cost on a portion of its variable-rate debt with an aggregate notional amount of \$6. The Company has designated these instruments as economic hedges accounted for at fair value with gains or losses recognized in interest, net. The net gain recognized by the Company was de minimis for the three months ended March 31, 2017 and 2016.

No ineffectiveness was recognized for the three months ended March 31, 2017 and 2016 related to hedging instruments.

The following table provides a summary of the gross fair value for the Company's derivative asset and liabilities, as well as the location of the asset and liability balances in the Consolidated Balance Sheets:

Derivative Instruments	Derivative Designation	Balance Sheet Classification	March	
			31, 2017	December 31, 2016
Asset Derivative				
Forward starting swaps	Cash flow hedge	Other current assets	\$ 31	\$ 27
Forward starting swaps	Cash flow hedge	Other long-term assets	1	—
Interest rate swap	Fair value hedge	Other current assets	1	1
Liability Derivative				
		Current portion of long-term		
Interest rate swap	Fair value hedge	debt	\$ 1	\$ 1

Note 6: Income Taxes

The Company's effective income tax rate was 35.9% and 39.7% for the three months ended March 31, 2017 and 2016, respectively. The effective income tax rate for the three months ended March 31, 2017 was impacted by a \$5 tax benefit from the new accounting standard for employee share-based payment awards which was adopted in 2017. Under this updated guidance, tax benefits or shortfalls related to employee share-based payment awards are recognized in the provision for income taxes, whereas they previously were recorded as additional paid-in capital on the Consolidated Balance Sheets. See Note 2—New Accounting Standards in the Notes to Consolidated Financial Statements for further discussion on the impacts of the updated guidance.

On April 11, 2017, the State of New York enacted legislation that would increase the state income tax rate on the Company's taxable income attributable to New York. Manufacturers in New York are taxed at a lower income tax rate, and this legislation eliminated the production of water as a qualified manufacturing activity. The effective date of the legislation is January 1, 2018 and this future increase in the New York tax rate will cause the Company to book a one-time adjustment during the second quarter of 2017, increasing its state accumulated deferred income tax liability. An offsetting adjustment will be recorded to regulatory assets for the amount recoverable in future customer rates, with the remaining balance recorded to income tax expense.

Note 7: Pension and Other Postretirement Benefits

The following table provides the components of net periodic benefit costs:

For the
Three
Months
Ended
March 31,
2017 2016

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Components of net periodic pension benefit cost		
Service cost	\$9	\$8
Interest cost	20	20
Expected return on plan assets	(24)	(24)
Amortization of actuarial loss	9	7
Net periodic pension benefit cost	\$14	\$11
Components of net periodic other postretirement benefit cost		
Service cost	\$3	\$3
Interest cost	7	7
Expected return on plan assets	(7)	(6)
Amortization of prior service credit	(5)	(1)
Amortization of actuarial loss	3	1
Net periodic other postretirement benefit cost	\$1	\$4

The Company contributed \$10 to its defined benefit pension plans in the first three months of 2017 and expects to contribute \$30 during the remainder of 2017. In addition, the Company contributed \$1 for the funding of its other postretirement plans in the first three months of 2017 and expects to contribute \$5 during the remainder of 2017.

Note 8: Commitments and Contingencies

Contingencies

The Company is routinely involved in legal actions incident to the normal conduct of its business. As of March 31, 2017, the Company has accrued approximately \$138 of probable loss contingencies and has estimated that the maximum amount of losses associated with reasonably possible loss contingencies that can be reasonably estimated is \$28. For certain matters, claims and actions, the Company is unable to estimate possible losses. The Company believes that damages or settlements, if any, recovered by plaintiffs in such matters, claims or actions, other than as described in this Note 8, will not have a material adverse effect on the Company.

West Virginia Elk River Freedom Industries Chemical Spill

Background

On January 9, 2014, a chemical storage tank owned by Freedom Industries, Inc. leaked two substances, 4-methylcyclohexane methanol, or MCHM, and PPH/DiPPH, a mix of polyglycol ethers, into the Elk River near the West Virginia-American Water Company (“WVAWC”) treatment plant intake in Charleston, West Virginia. After having been alerted to the leak of MCHM by the West Virginia Department of Environmental Protection (“DEP”), WVAWC took immediate steps to gather more information about MCHM, augment its treatment process as a precaution, and begin consultations with federal, state and local public health officials. As soon as possible after it was determined that the augmented treatment process would not fully remove the MCHM, a joint decision was reached in consultation with the West Virginia Bureau for Public Health to issue a “Do Not Use” order for all of its approximately 93,000 customer accounts in parts of nine West Virginia counties served by the Charleston treatment plant. By January 18, 2014, none of WVAWC’s customers were subject to the Do Not Use order.

Following the Freedom Industries chemical spill, numerous lawsuits were filed against WVAWC and certain other Company affiliated entities (collectively, the “American Water Defendants”) with respect to this matter in the U.S. District Court for the Southern District of West Virginia or West Virginia Circuit Courts in Kanawha, Boone and Putnam counties, and to date, 74 cases remain pending. Four of the cases pending before the U.S. district court were consolidated for purposes of discovery, and an amended consolidated class action complaint for those cases (the “Federal action”) was filed in December 2014 by several plaintiffs. On January 28, 2016, all of the then-filed state court cases were referred to West Virginia’s Mass Litigation Panel for further proceedings, which have been stayed pending the negotiation by the parties and approval by the court in the Federal action of a global agreement to settle all of such cases, as described below. On July 7, 2016, the court in the Federal action scheduled trial to begin on October 25, 2016, but the court has granted several continuances of the trial, which is currently postponed until June 6, 2017 and remains subject to further delay in light of the binding global agreement in principle described below. The Mass Litigation Panel has also stayed its proceedings until July 26, 2017.

WVAWC Binding Global Agreement in Principle to Settle Claims

On October 31, 2016, the court in the Federal action approved the preliminary principles, terms and conditions of a binding global agreement in principle to settle claims (the “Settlement”) among the American Water Defendants, and all class members, putative class members, claimants and potential claimants (collectively, the “Plaintiffs”), arising out of the Freedom Industries chemical spill. The terms of the Settlement propose a global federal and state resolution of all litigation and potential claims against the American Water Defendants and their insurers. A claimant may elect to opt out of any final settlement agreement, in which case such claimant will not receive any benefit from or be bound by the terms of the Settlement. Under the terms and conditions of the Settlement and any subsequent final settlement agreement, the American Water Defendants have not admitted, and will not admit, any fault or liability for any of the

allegations made by the Plaintiffs in any of the actions to be resolved.

The proposed aggregate pre-tax amount of the Settlement is \$126, of which \$65 would be contributed by WVAWC, and the remainder would be contributed by certain of the Company's general liability insurance carriers. The Company has general liability insurance under a series of policies underwritten by a number of individual carriers. Two of these insurance carriers, which provide an aggregate of \$50 in insurance coverage to the Company under these policies, were requested, but presently have not agreed, to participate in the Settlement. The Company and WVAWC are vigorously pursuing their rights to insurance coverage from these non-participating carriers for any contributions by WVAWC to the Settlement. In this regard, WVAWC filed a lawsuit against one of these carriers alleging that the carrier's failure to agree to participate in the Settlement constitutes a breach of contract, and the Company is pursuing mandatory arbitration against the other non-participating carrier.

The preliminary terms of the Settlement intend to establish a two-tier settlement fund for the payment of claims, comprised of (i) a simple claim fund, which is also referred to as the "guaranteed fund," of \$76, of which \$51 will be contributed by WVAWC, including insurance deductibles, and \$25 would be contributed by one of the Company's general liability insurance carriers, and (ii) an individual review claim fund of up to \$50, of which up to \$14 would be contributed by WVAWC and \$36 would be contributed by a

number of the Company's general liability insurance carriers. Separately, up to \$25 would be contributed to the guaranteed fund by another defendant to the Settlement.

As a result of these events, the Company recorded a charge to earnings, net of insurance receivables, of \$65 (\$39 after-tax) in the third quarter of 2016. The settlement amount of \$126 is reflected in Accrued Liabilities and the offsetting insurance receivable is reflected in Other Current Assets in the Consolidated Balance Sheet as of March 31, 2017. The Company intends to fund WVAWC's contributions to the Settlement through existing sources of liquidity, although no contribution by WVAWC will be required unless and until the terms of the Settlement are finally approved by the court in the Federal action. Furthermore, under the terms of the Settlement, WVAWC has agreed that it will not seek rate recovery from the Public Service Commission of West Virginia for approximately \$4 in direct response costs expended in 2014 by WVAWC relating to the Freedom Industries chemical spill as well as for amounts paid by WVAWC under the Settlement.

The Company's insurance policies operate under a layered structure where coverage is generally provided in the upper layers after claims have exhausted lower layers of coverage. The \$36 to be contributed by a number of the Company's general liability insurance carriers to the individual review claim fund, as noted above, is from higher layers of the insurance structure than the two insurance carriers that were requested, but presently have not agreed, to participate in the Settlement. Any recovery by WVAWC or the Company from the non-participating carriers would reimburse WVAWC for its contributions to the guaranteed fund.

On April 27, 2017, the parties filed with the court in the Federal action a proposed settlement agreement providing details of the terms of the Settlement consistent with those described above. The parties also requested that the court in the Federal action grant preliminary approval of the Settlement. If and when preliminary approval of the Settlement is obtained, notice of the terms of the Settlement would then be provided to members of the settlement class. Following the notice period, the court in the Federal action would hold a fairness hearing to consider final approval of the Settlement.

Other Related Proceedings

Additionally, investigations with respect to the matter have been initiated by the U.S. Chemical Safety and Hazard Investigation Board (the "CSB"), the U.S. Attorney's Office for the Southern District of West Virginia, the West Virginia Attorney General, and the Public Service Commission of West Virginia (the "PSC"). As a result of the U.S. Attorney's Office investigation, Freedom Industries and six former Freedom Industries employees (three of whom also were former owners of Freedom Industries), pled guilty to violations of the federal Clean Water Act.

In May 2014, the PSC issued an Order initiating a General Investigation into certain matters relating to WVAWC's response to the Freedom Industries chemical spill. Three parties intervened in the proceeding, including the Consumer Advocate Division of the PSC and two attorney-sponsored groups, including one sponsored by some of the plaintiffs' counsel involved in the civil litigation described above. On January 26, 2017, WVAWC and the other parties agreed to resolve the General Investigation and filed a joint stipulation with the PSC containing the terms of the settlement. The parties to the joint stipulation filed a proposed order with the PSC on February 8, 2017.

The CSB is an independent investigatory agency with no regulatory mandate or ability to issue fines or citations; rather, the CSB can only issue recommendations for further action. In response to the Freedom Industries chemical spill, the CSB commenced an investigation shortly thereafter. On September 28, 2016, the CSB issued and adopted its investigation report in which it recommended that the Company conduct additional source water protection activities. The Company provided written comments to the CSB's report suggesting that the recommendation made to the Company would be better directed to the U.S. Environmental Protection Agency in order to promote industry-wide implementation of the CSB's recommendation. On February 15, 2017, the Company filed a response to the CSB's

recommendation. On April 4, 2017, the CSB indicated that the implementation by the Company of source water protection activities resolved the first two parts of the CSB's recommendation. The CSB also noted that compliance by the Company with the third part of its recommendation is ongoing and that closure of this part is contingent upon completion of updated contingency planning for the Company's water utilities outside of West Virginia.

On March 16, 2017, the Lincoln County (West Virginia) Commission (the "LCC") passed a county ordinance entitled the "Lincoln County, WV Comprehensive Public Nuisance Investigation and Abatement Ordinance." The ordinance establishes a mechanism that Lincoln County believes will allow it to pursue criminal or civil proceedings for the "public nuisance" it alleges was caused by the Freedom Industries chemical spill. On April 20, 2017, the LCC filed a complaint in Lincoln County state court against WVAWC and certain other defendants not affiliated with the Company, alleging that the Freedom Industries chemical spill caused a public nuisance in Lincoln County. The complaint seeks an injunction against WVAWC that would require the creation of various databases and public repositories of documents related to this chemical spill, as well as further study and risk assessments regarding the alleged exposure by Lincoln County residents to the released chemicals. WVAWC believes that the lawsuit is without merit and intends to vigorously contest the claims and allegations raised in the complaint.

California Public Utilities Commission Residential Rate Design Proceeding

In December 2016, the California Public Utilities Commission (the “CPUC”) issued a final decision in a proceeding involving California-American Water Company, the Company’s wholly owned subsidiary (“Cal Am”), adopting a new residential rate design for Cal Am’s Monterey District. The decision allowed for recovery by Cal Am of \$32 in under-collections in the water revenue adjustment mechanism/modified cost balancing account (“WRAM/MCBA”) over a five-year period, plus interest, and modified existing conservation and rationing plans. In its decision, the CPUC noted concern regarding Cal Am’s residential tariff administration, specifically regarding the lack of verification of customer-provided information about the number of residents per household. This information was used for generating billing determinants under the tiered rate system. As a result, the CPUC kept this proceeding open to address several issues, including whether Cal Am’s residential tariff administration violated a statute, rule or CPUC decision, and if so, whether a penalty should be imposed.

On February 24, 2017, Cal Am, the Monterey Peninsula Water Management District, the CPUC’s Office of Ratepayer Advocates, and the Coalition of Peninsula Businesses filed for CPUC approval of a joint settlement agreement (the “Joint Settlement Agreement”), which among other things, proposed to resolve the CPUC’s residential tariff administration concerns by providing for a waiver by Cal Am of \$0.5 of cost recovery for residential customers through the WRAM/MCBA in lieu of a penalty. Approval of the Joint Settlement Agreement, which is required for it to take effect, remains pending before the CPUC.

On March 28, 2017, the administrative law judge assigned to the proceeding issued a ruling stating there was sufficient evidence to conclude, on a preliminary basis, that Cal Am’s administration of the residential tariff violated certain provisions of the California Public Utilities Code and a CPUC decision. The ruling ordered Cal Am to show cause why it should not be penalized for these administrative violations and directed the settling parties to address whether the cost recovery waiver in the Joint Settlement Agreement was reasonable compared to a potential penalty range described by the administrative law judge. During hearings held on April 13-14, 2017, the administrative law judge clarified that this potential penalty range is \$3 to \$179 (calculated as a continuing violation dating back to 2000 and applying penalties of up to \$20 thousand per day until January 1, 2012 and penalties of up to \$50 thousand per day thereafter, reflecting a 2012 change to the relevant statute). The administrative law judge also noted that a per diem penalty may not be appropriate, as Cal Am’s monthly billing practices did not allow Cal Am to update customer-provided information for billing purposes on a daily basis. The administrative law judge has set further hearings in this proceeding for August 17, 2017, and has permitted certain of the parties, including Cal Am, to submit additional written testimony on the issue of whether Cal Am should be penalized, and if so, the reasonable amount of any such penalty.

As of March 31, 2017, the portions of this loss contingency that are probable and/or reasonable possible have been determined to be immaterial to the Company and have been included in the aggregate maximum amounts described above in this Note 8.

Missouri Infrastructure System Replacement Surcharge Litigation

In March 2016, the Western District of the Missouri Court of Appeals ruled that the Missouri Public Service Commission (“MoPSC”) did not have statutory authority to issue an order in June 2015 approving an infrastructure system replacement surcharge (“ISRS”) for Missouri-American Water Company (“MAWC”), a wholly owned subsidiary of the Company. The court held that the MoPSC’s June 2015 order authorizing the ISRS increase was invalid because St. Louis County did not have a population of at least one million residents, as required by the statute. MAWC believes that the MoPSC’s June 2015 order authorizing the collection of ISRS revenues is lawful. In June 2016, the Missouri Supreme Court granted MAWC’s application to transfer the case from the Court of Appeals to the Missouri Supreme Court, and as a result of that order, the March 2016 ruling of the Court of Appeals was vacated.

On March 14, 2017, in a unanimous decision, the Missouri Supreme Court dismissed the case as moot, finding that there were no longer any ISRS funds in dispute because MAWC had completed a rate case during the appellate process and the disputed charges were now incorporated in base rates. On March 29, 2017, the Missouri Office of Public Counsel filed a Motion for Rehearing with the Missouri Supreme Court, which remains pending.

As a result of the Missouri Supreme Court's decision, the Company has determined that, as of March 31, 2017, a loss associated with this matter is remote.

Note 9: Earnings per Common Share

The following is a reconciliation of the numerator and denominator for basic and diluted earnings per share (“EPS”) calculations:

	For the Three Months Ended March 31, 2017 2016	
Numerator		
Net income attributable to common stockholders	\$93	\$82
Denominator		
Weighted-average common shares outstanding—Basic	178	178
Effect of dilutive common stock equivalents	1	1
Weighted-average common shares outstanding—Diluted	179	179

The effect of dilutive common stock equivalents is related to restricted stock units and stock options granted under the 2007 Plan, and shares purchased under the Company’s Nonqualified Employee Stock Purchase Plan.

Note 10: Fair Value of Financial Assets and Liabilities

Fair Value of Financial Instruments

The Company used the following methods and assumptions to estimate its fair value disclosures for financial instruments:

Current assets and current liabilities—The carrying amounts reported in the accompanying Consolidated Balance Sheets for current assets and current liabilities, including revolving credit debt, due to the short-term maturities and variable interest rates, approximate their fair values.

Preferred stock with mandatory redemption requirements and long-term debt—The fair values of preferred stock with mandatory redemption requirements and long-term debt are categorized within the fair value hierarchy based on the inputs that are used to value each instrument. The fair value of long-term debt classified as Level 1 is calculated using quoted prices in active markets. Level 2 instruments are valued using observable inputs and Level 3 instruments are valued using observable and unobservable inputs. The fair values of instruments classified as Level 2 and 3 are determined by a valuation model that is based on a conventional discounted cash flow methodology and utilizes assumptions of current market rates. As a portion of the Company’s debts do not trade in active markets, the Company calculated a base yield curve using a risk-free rate (a U.S. Treasury securities yield curve) plus a credit spread that is based on the following two factors: (i) an average of the Company’s own publicly-traded debt securities and (ii) the current market rates for U.S. Utility A debt securities. The Company used these yield curve assumptions to derive a base yield for the Level 2 and Level 3 securities. Additionally, the Company adjusted the base yield for specific features of the debt securities including call features, coupon tax treatment and collateral for the Level 3 instruments.

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The carrying amounts, including fair value adjustments previously recognized in acquisition purchase accounting and a fair value adjustment related to the Company's interest rate swap fair value hedge (which is classified as Level 2 in the fair value hierarchy), and fair values of the financial instruments were as follows:

	Carrying Amount	At Fair Value as of March 31, 2017			Total
		Level 1	Level 2	Level 3	
Preferred stock with mandatory redemption requirements	\$ 11	\$—	\$—	\$ 14	\$ 14
Long-term debt (excluding capital lease obligations)	6,316	3,972	1,363	1,822	7,157

	Carrying Amount	At Fair Value as of December 31, 2016			Total
		Level 1	Level 2	Level 3	
Preferred stock with mandatory redemption requirements	\$ 12	\$—	\$—	\$ 15	\$ 15
Long-term debt (excluding capital lease obligations)	6,320	3,876	1,363	1,805	7,044

Recurring Fair Value Measurements

The following table presents assets and liabilities measured and recorded at fair value on a recurring basis and their level in the fair value hierarchy:

	At Fair Value as of March 31, 2017			Total
	Level 1	Level 2	Level 3	
Assets:				
Restricted funds	\$28	\$ —	\$ —	\$ 28
Rabbi trust investments	13	—	—	13
Deposits	4	—	—	4
Mark-to-market derivative assets	—	33	—	33
Other investments	4	—	—	4
Total assets	49	33	—	82
Liabilities:				
Deferred compensation obligations	15	—	—	15
Mark-to-market derivative liabilities	—	—	—	—
Total liabilities	15	—	—	15
Total net assets (liabilities)	\$34	\$ 33	\$ —	\$ 67

	At Fair Value as of December 31, 2016			Total
	Level 1	Level 2	Level 3	
Assets:				
Restricted funds	\$24	\$ —	\$ —	\$ 24
Rabbi trust investments	12	—	—	12
Deposits	3	—	—	3
Mark-to-market derivative assets	—	28	—	28
Other investments	1	—	—	1
Total assets	40	28	—	68
Liabilities:				
Deferred compensation obligations	13	—	—	13
Mark-to-market derivative liabilities	—	—	—	—
Total liabilities	13	—	—	13
Total net assets (liabilities)	\$27	\$ 28	\$ —	\$ 55

Restricted funds—The Company's restricted funds primarily represent proceeds received from financings for the construction and capital improvement of facilities and from customers for future services under operations and maintenance projects. The proceeds of these financings are held in escrow until the designated expenditures are incurred. Long-term restricted funds of \$4 were included in other long-term assets as of March 31, 2017 and

December 31, 2016.

Rabbi trust investments—The Company’s rabbi trust investments consist of equity and index funds from which supplemental executive retirement plan benefits and deferred compensation obligations can be paid. The Company includes these assets in other long-term assets.

Deposits—Deposits include escrow funds and certain other deposits held in trust. The Company includes cash deposits in other current assets.

Deferred compensation obligations—The Company’s deferred compensation plans allow participants to defer certain cash compensation into notional investment accounts. The Company includes such plans in other long-term liabilities. The value of the Company’s deferred compensation obligations is based on the market value of the participants’ notional investment accounts. The notional investments are comprised primarily of mutual funds, which are based on observable market prices.

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Mark-to-market derivative asset and liability—The Company utilizes fixed-to-floating interest-rate swaps, typically designated as fair-value hedges, to achieve a targeted level of variable-rate debt as a percentage of total debt. The Company also employs derivative financial instruments in the form of variable-to-fixed interest rate swaps and forward starting interest rate swaps, classified as economic hedges and cash flow hedges, respectively, in order to fix the interest cost on existing or forecasted debt. The Company uses a calculation of future cash inflows and estimated future outflows, which are discounted, to determine the current fair value. Additional inputs to the present value calculation include the contract terms, counterparty credit risk, interest rates and market volatility.

Other investments—Other investments primarily represent money market funds used for active employee benefits. The Company includes other investments in other current assets.

Note 11: Segment Information

The Company operates its businesses primarily through one reportable segment, the Regulated Businesses segment. The Company also operates businesses that provide a broad range of related and complementary water and wastewater services in non-regulated markets, which includes four operating segments that individually do not meet the criteria of a reportable segment. These four non-reportable operating segments are collectively presented as our “Market-Based Businesses”. “Other” includes corporate costs that are not allocated to the Company’s operating segments, eliminations of inter-segment transactions, fair value adjustments and associated income and deductions related to acquisitions that have not been allocated to the operating segments for evaluation of performance and allocation of resource purposes. The following tables include the Company’s summarized segment information:

	As of or for the Three Months Ended March 31, 2017			
	Regulated		Market-Based	
	Businesses	Businesses	Other	Consolidated
Operating revenues	\$659	\$ 103	\$(6)	\$ 756
Depreciation and amortization	117	4	3	124
Total operating expenses, net	441	94	(6)	529
Interest, net	66	—	19	85
Income from continuing operations before income taxes	154	10	(19)	145
Provision for income taxes	60	3	(11)	52
Net income attributable to common stockholders	94	7	(8)	93
Total assets	16,632	555	1,423	18,610

	As of or for the Three Months Ended March 31, 2016			
	Regulated		Market-Based	
	Businesses	Businesses	Other	Consolidated
Operating revenues	\$634	\$ 114	\$(5)	\$ 743
Depreciation and amortization	108	3	5	116
Total operating expenses, net	430	104	(5)	529
Interest, net	64	—	16	80
Income from continuing operations before income taxes	143	10	(17)	136

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Provision for income taxes	56	4	(6)	54
Net income attributable to common stockholders	87	6	(11)	82
Total assets	15,472	512	1,433	17,417

ITEM 2.MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion should be read together with the unaudited consolidated financial statements and the notes thereto included elsewhere in this Form 10-Q. This discussion contains forward-looking statements that are based on management’s current expectations, estimates and projections about our business, operations and financial performance. The cautionary statements made in this Form 10-Q should be read as applying to all related forward-looking statements whenever they appear in this Form 10-Q. Our actual results may differ materially from those currently anticipated and expressed in such forward-looking statements as result of a number of factors, including those we discuss under “Forward Looking Statements,” and elsewhere in this Form 10-Q.

General

Through its subsidiaries, American Water Works Company, Inc. (“American Water” or the “Company”) is the largest and most geographically diverse investor-owned publicly-traded water and wastewater utility company in the United States, as measured by both operating revenue and population served. Our primary business involves the ownership of utilities that provide water and wastewater services to residential, commercial, industrial and other customers, including sale for resale and public authority customers. Our utilities are generally subject to economic regulation by certain state utility commissions or other entities engaged in utility regulation. We report the results of our utilities in our Regulated Businesses segment. We also operate several businesses that provide a broad range of related and complementary water and wastewater services that are not subject to economic regulation by state utility commissions or other entities engaged in utility regulation. We present the results of these businesses as our “Market-Based Businesses”. For further description of our businesses, see Part I, Item 1—Business in our Form 10-K.

You should read the following discussion in conjunction with our Consolidated Financial Statements and related Notes included elsewhere in this Form 10-Q and in our Form 10-K.

Financial Results

Income attributable to common stockholders was \$93 million, or \$0.52 per diluted share for the first quarter of 2017, an increase of 13% over the same period in 2016. This increase was primarily due to continued growth in our Regulated Businesses segment, largely attributable to additional authorized revenue driven by investment growth, acquisitions and organic growth, and a tax benefit associated with the new accounting standard requirements for stock-based compensation.

See “Comparison of Consolidated Results of Operations” and “Segment Results of Operations” below for further discussion on the consolidated results of operations, as well as our business segments.

Focusing on Central Themes

For 2017, our focus continues to be anchored on our five central themes: 1) Safety, 2) Customers, 3) People, 4) Growth and 5) Technology and Operational Efficiency. We continue our focus on operating our business responsibly and managing our operating and capital costs in a manner that benefits our customers and produces long-term value for our stockholders. Additionally, we continue to execute on our ongoing strategy that ensures a safe workplace for our employees, emphasizes public safety for our customers and communities, and leverages our human resources, processes and technology innovation to make our business more effective and efficient. The progress that we have made in the first three months of 2017 with respect to growth and improvement in our operational efficiency ratio is described below.

Growth—Infrastructure improvements, acquisitions and strategic capital investments

During the first three months of 2017, we made capital investments of approximately \$242 million, the majority of which was in our Regulated Businesses, primarily to improve infrastructure. For the full year of 2017, our total capital investment, including acquisitions, is expected to be approximately \$1.5 billion, most of which is allocated to improving infrastructure in our Regulated Businesses.

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Regulated acquisition growth included:

• Closed acquisitions of \$38 million, adding approximately 13,000 customers through May 3, 2017. This includes the acquisition on April 3, 2017, of all of the outstanding capital stock of Shorelands Water Company, Inc. (“Shorelands”), for total consideration of \$33 million in the form of 438,211 shares of our common stock. Shorelands provides water service to approximately 11,000 customers in Monmouth County, New Jersey. The assets acquired are owned by New Jersey-American Water Company, Inc.

• Pending acquisitions representing the addition of approximately 33,000 customers, including the September 9, 2016, asset purchase agreement signed by Pennsylvania-American Water Company to acquire substantially all of the wastewater collection and treatment system assets of the Municipal Authority of the City of McKeesport, Pennsylvania for approximately \$156 million, subject to certain adjustments provided in the agreement. In connection with the execution of this agreement, a \$7 million non-escrowed deposit has been made to the seller. The closing of this acquisition is subject to the satisfaction of various conditions and covenants, including obtaining the approval of the Pennsylvania Public Utility Commission. The system currently represents approximately 22,000 wastewater customers. We are expecting to close this acquisition in the fourth quarter of 2017.

Technology & Operational Efficiency—Continuing Improvement in Adjusted Operation and Maintenance (“O&M”) Efficiency Ratio for our Regulated Businesses

We continued to improve on our adjusted O&M efficiency ratio (a non-GAAP measure). Our adjusted O&M efficiency ratio for the twelve months ended March 31, 2017 was 34.6%, compared to 35.6% for the twelve months ended March 31, 2016. The improvement in the 2017 O&M efficiency ratio over this period was attributable to an increase in revenue.

Our adjusted O&M efficiency ratio is defined as our regulated O&M expenses divided by regulated operating revenues, where both O&M expenses and operating revenues were adjusted to eliminate purchased water expense. Additionally, from the O&M expenses, we excluded the allocable portion of non-O&M support services cost, mainly depreciation and general taxes that are reflected in the Regulated Businesses segment as O&M expenses but for consolidated financial reporting purposes are categorized within other line items in the accompanying Consolidated Statements of Operations. In addition to the standard adjustments to the O&M efficiency ratio for the twelve months ended March 31, 2017, we have also excluded from O&M expenses, the impact from the binding global agreement in principle related to the Freedom Industries chemical spill in West Virginia. We excluded all the above items from the calculation as we believe such items are not reflective of management’s ability to increase efficiency of the Company’s regulated operations.

We evaluate our operating performance using this measure because we believe it is a direct measure of the improvement to the efficiency of our regulated operations. This information is intended to enhance an investor’s overall understanding of our operating performance. The O&M efficiency ratio is not a GAAP financial measure and may not be comparable to other companies’ operating measures and should not be used in place of the GAAP information provided elsewhere in this report.

The following table provides the calculation and reconciliation that compares O&M expenses and operating revenues, as determined in accordance with GAAP, to those amounts utilized in the calculation of our adjusted O&M efficiency ratio for the twelve months ended March 31, 2017, as compared to the same period in 2016:

(In millions)	For the Twelve Months Ended March 31,	
	2017	2016
Total operation and maintenance expenses	\$ 1,493	\$ 1,428
Less:		
Operation and maintenance expenses—Market-Based Businesses	361	383
Operation and maintenance expenses—Other	(44)	(46)
Total operation and maintenance expenses—Regulated Businesses	1,176	1,091
Less:		
Regulated purchased water expenses	122	116
Allocation of non-operation and maintenance expenses	28	33
Impact of binding global agreement in principle	65	—
Adjusted operation and maintenance expenses—Regulated Businesses (a)	\$ 961	\$ 942
Total operating revenues	\$ 3,315	\$ 3,204
Less:		
Operating revenues—Market-Based Businesses	440	461
Operating revenues—Other	(21)	(19)
Total regulated operating revenues—Regulated Businesses	2,896	2,762
Less:		
Regulated purchased water revenues*	122	116
Adjusted operating revenues—Regulated Businesses (b)	\$ 2,774	\$ 2,646
Adjusted operation and maintenance efficiency ratio—Regulated Businesses	34.6 %	35.6 %

(a)/(b)

*Calculation assumes purchased water revenues approximate purchased water expenses.

Regulatory Matters

The table below provides rate authorizations which became effective during the three months ended March 31, 2017. The table depicts annualized incremental revenues, assuming a constant water sales volume, resulting from general rate cases and, infrastructure surcharge mechanisms that became effective during the period:

(In millions)	For the Three Months Ended March 31, 2017
General rate cases by state:	
Illinois (January 1)	\$ 25
California (January 13)	5
Iowa (March 27)	4
Total general rate cases	\$ 34
Infrastructure surcharges by state:	
West Virginia (January 1)	\$ 2
Pennsylvania (January 1)	1
Tennessee (March 14)	2
Indiana (March 22)	8
Total infrastructure surcharges	\$ 13

Pending and Filed Rate Cases

On April 3, 2017, our California subsidiary filed a cost of capital application requesting a return on equity of 10.8%. The results of this proceeding will not become effective until January 2018.

On April 13, 2017, our New Jersey subsidiary filed for an infrastructure surcharge requesting additional revenues of \$10 million.

On April 28, 2017, our Pennsylvania subsidiary filed a general rate case requesting \$108 million in additional annualized water and wastewater revenues.

In addition to the filings discussed above, we are awaiting final general rate case orders in three states requesting additional annualized revenue of \$52 million. One of these states authorized interim rates under bond, subject to refund, which were put into effect in 2016. We are also awaiting approval in one state for a step rate and attrition rate increase of \$8 million in both 2019 and 2020. There is no assurance that all or any portion of these requests will be granted.

Other Regulatory Matters

On April 5, 2017, Senate Bill 1492 impacting our Virginia subsidiary was approved and will become law later in 2017. The new law directs the Virginia State Corporation Commission to require water and wastewater utilities in any proceeding after July 1, 2017, to consolidate tariffs for each service statewide.

Other Tax Matters

On April 11, 2017, the State of New York enacted legislation that would increase the state income tax rate on our taxable income attributable to New York. Manufacturers in New York are taxed at a lower income tax rate, and this legislation eliminated the production of water as a qualified manufacturing activity. The effective date of the legislation is January 1, 2018 and this future increase in the New York tax rate will cause us to book a one-time adjustment during the second quarter of 2017, increasing our state accumulated deferred income tax liability. An offsetting adjustment will be recorded to regulatory assets for the amount recoverable in future customer rates, with the remaining balance, preliminarily estimated to be between \$5 million and \$7 million, recorded to income tax expense.

Consolidated Results of Operations

(In millions)	For the Three Months Ended March 31,			
	2017	2016	Increase (Decrease) %	
Operating revenues	\$756	\$743	\$13	1.7
Operating expenses:				
Operation and maintenance	337	348	(11)	(3.2)
Depreciation and amortization	124	116	8	6.9
General taxes	68	66	2	3.0
Gain on asset dispositions and purchases	—	(1)	1	(100.0)
Total operating expenses, net	529	529	—	—
Operating income	227	214	13	6.1
Other income (expenses):				
Interest, net	(85)	(80)	(5)	6.3
Other, net	3	2	1	50.0
Total other income (expenses)	(82)	(78)	(4)	5.1
Income from continuing operations before income taxes	145	136	9	6.6
Provision for income taxes	52	54	(2)	(3.7)
Net income attributable to common stockholders	\$93	\$82	\$11	13.4

Comparison of Consolidated Results of Operations

Operating revenues. For the three months ended March 31, 2017, operating revenues increased primarily due to a:

\$25 million increase in our Regulated Businesses segment principally due to authorized rate increases to fund infrastructure investment growth, acquisitions and organic growth, partially offset by lower demand and consumption when compared to the same period in 2016; and

\$11 million decrease in our Market-Based Businesses primarily due to lower revenue from capital upgrades in our Military Services Group as a result of the completion of a large project in mid-2016 at Fort Polk and reduced military base budgets. Partially offsetting this decrease were incremental revenues from our Homeowner Services Group from customer additions and price increases.

Operation and maintenance. For the three months ended March 31, 2017, operation and maintenance expense decreased principally due to a:

\$11 million decrease in our Market-Based Businesses attributable to lower capital upgrades in our Military Services Group corresponding with the decrease in operating revenues discussed above, partially offset by higher expenses in our Homeowner Services Group due to higher claims expense.

Depreciation and amortization. For the three months ended March 31, 2017, depreciation and amortization expense increased largely due to additional utility plant placed in service.

Other income (expenses). For the three months ended March 31, 2017, other expenses increased primarily due to an increase in long-term interest expense from the issuance of incremental long-term debt in the fourth quarter of 2016, as well as an increase in short-term interest expense resulting from higher levels of short-term borrowings, coupled with an increase in the average short-term borrowing rates.

Provision for income taxes. For the three months ended March 31, 2017, our provision for income taxes decreased principally due to the tax benefit recorded as a result of the new accounting standard for stock-based compensation.

Segment Results of Operations

Our segments are determined based on how we assess performance and allocate our resources. We evaluate the performance of our segments and allocate resources based on several factors, with the primary measure being income from continuing operations.

We conduct our business primarily through one reportable segment, our Regulated Businesses segment. We also operate businesses that provide a broad range of related and complementary water and wastewater services, which includes four operating segments that individually do not meet the criteria of a reportable segment. These four non-reportable segments have been combined and are presented as our “Market-Based Businesses”, which is consistent with how management assesses the results of our businesses.

Regulated Businesses Segment

The following table summarizes certain financial information for our Regulated Businesses segment:

(In millions)	For the Three Months Ended March 31,			
	2017	2016	Increase (Decrease)	%
Operating revenues	\$659	\$634	\$ 25	3.9
Operation and maintenance	262	262	—	—
Total operating expenses, net	441	430	11	2.6
Net income attributable to common stockholders	94	87	7	8.0

Operating revenues. The following tables and discussions provide explanation of the variances related to the three components of operating revenues—water services revenues, wastewater services revenues and other revenues:

(In millions)	For the Three Months Ended March 31,			
	2017	2016	Increase (Decrease)	%
Billed water services:				
Residential	\$364	\$348	\$16	4.6
Commercial	129	125	4	3.2
Industrial	32	30	2	6.7
Public and other	81	76	5	6.6
Other water revenues	15	11	4	36.4
Billed water services	621	590	31	5.3
Unbilled water services	(7)	5	(12)	(240.0)
Total water services revenues	614	595	19	3.2
Wastewater services revenues	34	27	7	25.9
Other revenues	11	12	(1)	(8.3)
Total operating revenues	\$659	\$634	\$25	3.9

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(In millions)	For the Three Months Ended March 31,		Increase (Decrease)	
	2017	2016		%
Billed water services volumes:				
Residential	35,985	36,409	(424)	(1.2)
Commercial	17,063	17,416	(353)	(2.0)
Industrial	8,878	8,640	238	2.8
Public and other	11,493	10,968	525	4.8
Billed water services volumes	73,419	73,433	(14)	(0.0)

For the three months ended March 31, 2017, operating revenues increased primarily due to a:

- \$25 million increase from authorized rate increases, including infrastructure surcharges, to fund infrastructure investment growth in various states;
- \$8 million increase resulting from water and wastewater acquisitions as well as organic growth in existing systems; and
- \$7 million decrease in demand and consumption when compared to the same period in 2016.

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Operation and maintenance. The following table summarizes information regarding the components of operation and maintenance expense:

(In millions)	For the Three Months Ended			
	March 31,		Increase (Decrease)	
	2017	2016		%
Production costs	\$63	\$63	\$ —	—
Employee-related costs	111	109	2	1.8
Operating supplies and services	48	50	(2)	(4.0)
Maintenance materials and supplies	18	15	3	20.0
Customer billing and accounting	10	14	(4)	(28.6)
Other	12	11	1	9.1
Total	\$262	\$262	\$ —	—

For the three months ended March 31, 2017, operation and maintenance expense was flat when compared to the same period in 2016. Variances related to individual components of operation and maintenance expense include a:

\$4 million decrease in customer billing and accounting due to a reduction in uncollectible expense primarily attributable to focused collection efforts; and

\$3 million increase in maintenance materials and supplies primarily due to increased tank painting costs, as well as the timing of specific maintenance activity in 2017 as compared to the same period in 2016;

Operating expenses, net. For the three months ended March 31, 2017, operating expenses, net increased primarily due to higher depreciation and amortization expense and general taxes expense of \$9 million and \$3 million, respectively. The increase in depreciation and amortization expense was driven by additional utility plant placed in service. The increase in general taxes is primarily due to higher gross receipts tax in New Jersey and higher property taxes in 2017 driven by investment growth.

Market-Based Businesses

The following table summarizes certain financial information for our Market-Based Businesses:

(In millions)	For the Three Months			
	Ended March 31,		Increase	
	2017	2016	(Decrease)	%
Operating revenues	\$103	\$114	\$(11)	(9.6)
Operation and maintenance	88	99	(11)	(11.1)
Total operating expenses, net	94	104	(10)	(9.6)
Net income attributable to common				
stockholders	7	6	1	16.7

Operating revenues. For the three months ended March 31, 2017, operating revenues decreased primarily due to a:

\$18 million decrease in our Military Services Group resulting from lower capital upgrades in 2017 compared to 2016 primarily attributable to reduced military base infrastructure budgets and the completion of a large project at Fort Polk in mid-2016; partially offset by a

\$5 million increase in our Homeowner Services Group primarily due to customer additions and price increases for certain existing customers.

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Operation and maintenance. The following table summarizes information regarding the components of operation and maintenance expense:

(In millions)	For the Three Months Ended March 31,			
	2017	2016	Increase (Decrease) %	
Production costs	\$10	\$9	\$1	11.1
Employee-related costs	24	24	-	-
Operating supplies and services	30	47	(17)	(36.2)
Maintenance materials and supplies	21	16	5	31.3
Other	3	3	—	—
Total	\$88	\$99	\$(11)	(11.1)

For the three months ended March 31, 2017, operation and maintenance expense decreased primarily due to a:

\$16 million decrease in operating supplies and services resulting from lower capital upgrades in our Military Services Group, as discussed above, and focused cost management in Keystone; partially offset by a \$5 million increase in maintenance services and supplies due principally to contract growth and incremental claims activity in our Homeowner Services Group.

Liquidity and Capital Resources

For a general overview of our sources and uses of capital resources, see the introductory discussion in Part II, Item 7—Management’s Discussion and Analysis of Financial Condition and Results of Operations—Liquidity and Capital Resources contained in our Form 10-K.

We fund liquidity needs for capital investment, working capital and other financial commitments through cash flows from operations, public and private debt offerings, commercial paper markets and, if and to the extent necessary, borrowing under the American Water Capital Corp. (“AWCC”) revolving credit facility. The revolving credit facility provides \$1.75 billion in aggregate total commitments from a diversified group of financial institutions with an expiration date of June 2020 (subject to extension by us for up to two one-year periods). We regularly evaluate the capital markets and closely monitor the financial condition of the financial institutions with contractual commitments in our revolving credit facility.

In order to meet our short-term liquidity needs, we, through AWCC, our wholly owned financing subsidiary, issue commercial paper, which is supported by our revolving credit facility. As of March 31, 2017, AWCC had no outstanding borrowings and \$86 million of outstanding letters of credit under the revolving credit facility, with \$1.66 billion available to fulfill our short-term liquidity needs and to issue letters of credit. As of March 31, 2017, the revolving credit facility supported \$980 million in outstanding commercial paper. We believe that our ability to access the capital markets, our revolving credit facility and our cash flows from operations will generate sufficient cash to fund our short-term requirements. However, we can provide no assurances that the lenders will meet their existing commitments to AWCC under the credit facility or that we will be able to access the commercial paper or loan markets in the future on terms acceptable to us or at all.

On February 8, 2017, we entered into a forward swap agreement with a notional amount of \$100 million to reduce interest rate exposure for a portion of the expected refinancing of our 5.62% fixed-rate long-term debt maturing in December 2018. This forward starting swap agreement terminates in November 2018 and has a fixed rate of 2.67%. During the three months ended March 31, 2017, the fair value of our five forward starting swaps increased by \$5 million due to higher forward interest rates. Changes in the fair value of the forward starting swaps will be recognized in accumulated other comprehensive loss until the agreements terminate. See Note 5—Long-Term Debt for further information.

Cash Flows Provided by Operating Activities

Cash flows provided by operating activities primarily result from the sale of water and wastewater services and, due to the seasonality of demand, are generally greater during the third quarter of each fiscal year. The following table provides a summary of the major items affecting cash flows provided by our operating activities:

	For the Three Months Ended March 31, 2017 2016	
(In millions)		
Net income	\$93	\$82
Add (less):		
Non-cash activities (a)	189	177
Changes in working capital (b)	6	15
Pension and postretirement healthcare contributions	(11)	(14)
Net cash flows provided by operations	\$277	\$260

(a) Includes depreciation and amortization, deferred income taxes and amortization of deferred investment tax credits, provision for losses on accounts receivable, gain on asset dispositions and purchases, pension and non-pension postretirement benefits expense and other non-cash, net. Details of each component can be found in the Consolidated Statements of Cash Flows.

(b) Changes in working capital include changes to receivables and unbilled revenues, accounts payable and accrued liabilities, and other current assets and liabilities, net.

For the three months ended March 31, 2017, the increase in cash flows from operating activities, as compared to the same period in 2016, is primarily due to an increase in net income after non-cash adjustments. The main factors contributing to net income increase are described in this section under “Comparison of Consolidated Results of Operations” and included higher operating revenue and lower operation and maintenance expense. The increase in non-cash activities was mainly the result of an increase in depreciation and amortization attributable to infrastructure investment projects placed into service. The change in working capital was primarily the result of the following: (1) timing of accounts payable and accrued liabilities; and (2) change in other current assets and liabilities.

Cash Flows Used in Investing Activities

The following table provides information regarding cash flows used in our investing activities:

	For the Three Months Ended March 31, 2017 2016	
(In millions)		

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Net capital expenditures	\$ (270)	\$ (284)
Acquisitions	(2)	(22)
Other investing activities, net (a)	(16)	(17)
Net cash flows used in investing activities	\$ (288)	\$ (323)

(a) Includes removal costs from property, plant and equipment retirements, net, proceeds from sale of assets and net funds restricted.

For the three months ended March 31, 2017, cash used in investing activities decreased primarily due to the timing of payments for the capital expenditures and acquisitions. We continue to expect investments of approximately \$1.5 billion in 2017 for capital expenditures and acquisitions. We have also begun the construction of our new corporate headquarters building in Camden, New Jersey. The cost of construction is currently estimated to be up to \$165 million, exclusive of any tax incentives, with \$77 million expected to be incurred in 2017.

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Cash Flows Provided by Financing Activities

The following table provides information regarding cash flows provided by our financing activities:

	For the Three Months Ended March 31, 2017 2016	
(In millions)		
Repayments of long-term debt	\$(4)	\$(11)
Net proceeds from short-term borrowings	131	211
Dividends paid	(67)	(61)
Anti-dilutive stock repurchases	(54)	(62)
Other financing activities, net (a)	8	7
Net cash flows provided by financing activities	\$ 14	\$ 84

(a) Includes proceeds from issuance of common stock under various employee stock plans and our dividend reinvestment plan, advances and contributions for construction, net of refunds and debt issuance costs.

For the three months ended March 31, 2017, the decrease in cash flows provided by financing activities, as compared to the same period in 2016, is primarily due to incremental short-term borrowings in 2016 to fund a portion of the capital expenditures and acquisitions.

Credit Facilities and Short-Term Debt

The following table summarizes information regarding our aggregate credit facility commitments, letter of credit sub-limits and available funds under those revolving credit facilities, as well as outstanding amounts of commercial paper and outstanding borrowings under the respective facilities as of March 31, 2017:

	Available Credit		Available Letter		Available	
Credit Facility	Facility	Letter of	of Credit	Commercial	Paper	Commercial
Commitments (a)	Capacity (a)	Credit	Capacity	Paper Limit	Paper Capacity	Paper Capacity
(In millions)						
March 31, 2017	\$ 1,766	\$ 1,673	\$ 150	\$ 64	\$ 1,600	\$ 620

(a) Includes amounts related to the revolving credit facility of Keystone Clearwater Solutions, LLC (“Keystone”), our water management solutions subsidiary. As of March 31, 2017, the total commitment under the Keystone revolving credit facility was \$16 million, of which \$9 million was available for borrowing, subject to compliance with a collateral base calculation.

The weighted-average interest rate on AWCC short-term borrowings for the three months ended March 31, 2017 and 2016 was approximately 1.02% and 0.74%, respectively.

Capital Structure

The following table indicates the percentage of our capitalization represented by the components of our capital structure as of the dates set forth below:

	March 31, 2017	%	December 31, 2016	%
Total common stockholders' equity	42.0	%	42.1	%
Long-term debt and redeemable preferred stock at redemption value	45.7	%	46.4	%
Short-term debt and current portion of long-term debt	12.3	%	11.5	%
	100	%	100	%

Debt Covenants

Our debt agreements contain financial and non-financial covenants. To the extent that we are not in compliance with these covenants, an event of default may occur under one or more debt agreements and we or our subsidiaries may be restricted in our ability to pay dividends, issue new debt or access our revolving credit facility. Our long-term debt indentures contain a number of covenants that, among other things, prohibit or restrict the Company from issuing debt secured by the Company's assets, subject to certain exceptions. Our failure to comply with any of these covenants could accelerate repayment obligations.

Covenants in certain long-term notes and the revolving credit facility require us to maintain a ratio of consolidated debt to consolidated capitalization (as defined in the relevant documents) of not more than 0.70 to 1.00. On March 31, 2017, our ratio was 0.58 to 1.00 and therefore we were in compliance with the covenants.

Security Ratings

Our access to the capital markets, including the commercial paper market, and respective financing costs in those markets, may be directly affected by our securities ratings. We primarily access the debt capital markets, including the commercial paper market, through AWCC. However, we have also issued debt through our regulated subsidiaries, primarily in the form of tax exempt securities or borrowings under state revolving funds, to lower our overall cost of debt.

Our long-term and short-term credit ratings as of March 31, 2017 are as follows:

	Moody's	Standard & Poor's
Securities	Investors Service	Ratings Service
Senior unsecured debt	A3	A
Commercial paper	P2	A-1

A security rating is not a recommendation to buy, sell or hold securities and may be subject to revision or withdrawal at any time by the assigning rating agency, and each rating should be evaluated independently of any other rating. Security ratings are highly dependent upon our ability to generate cash flows in an amount sufficient to service our debt and meet our investment plans. We can provide no assurances that our ability to generate cash flows is sufficient to maintain our existing ratings. None of our borrowings are subject to default or prepayment as a result of a downgrading of these security ratings, although such a downgrading could increase fees and interest charges under our credit facility.

Dividends

On March 1, 2017, we paid a cash dividend of \$0.375 per share to our stockholders of record as of February 7, 2017.

On April 21, 2017, our Board of Directors declared a quarterly cash dividend payment of \$0.415 per share payable on June 1, 2017 to stockholders of record as of May 5, 2017. Future dividends, when and as declared at the discretion of the Board of Directors, will be dependent upon future earnings and cash flows, compliance with various regulatory, financial and legal requirements, and other factors. See Part II, Item 7—Management’s Discussion and Analysis of Financial Condition and Results of Operations—Liquidity and Capital Resources—Dividends in our Form 10-K for more information regarding restrictions on the payment of dividends on our common stock.

Application of Critical Accounting Policies and Estimates

Our financial condition, results of operations and cash flows are impacted by the methods, assumptions and estimates used in the application of critical accounting policies. See Part II, Item 7—Management’s Discussion and Analysis of Financial Condition and Results of Operations—Critical Accounting Policies and Estimates in our Form 10-K for a discussion of our critical accounting policies.

Recent Accounting Standards

See Note 2—New Accounting Standards to the Notes to Consolidated Financial Statements included in Part I, Item 1—Consolidated Financial Statements of this Quarterly Report on Form 10-Q for a description of new accounting standards recently adopted or pending adoption.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We are subject to market risks in the normal course of business, including changes in interest rates and equity prices. For a discussion of our exposure to market risk, refer to Part II, Item 7A—Quantitative and Qualitative Disclosures about Market Risk contained in our Form 10-K. Except as described below, there have been no significant changes to our exposure to market risk since December 31, 2016.

On February 8, 2017, we entered into a forward starting swap agreement with a notional amount of \$100 million to reduce interest rate exposure on debt expected to be issued in 2018. This forward starting swap agreement terminates in November 2018 and

has an average fixed rate of 2.67%. A hypothetical one hundred basis point change in the forward starting swap rates would have resulted in a \$19 million increase or decrease in fair value for the three months ended March 31, 2017.

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

American Water maintains disclosure controls and procedures that are designed to ensure that information required to be disclosed in its reports filed or submitted under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to management, including the Chief Executive Officer and the Chief Financial Officer, to allow timely decisions regarding required disclosure. In designing and evaluating the disclosure controls and procedures, management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives.

Our management, including the Chief Executive Officer and the Chief Financial Officer, conducted an evaluation of the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) of the Exchange Act) as of March 31, 2017.

Based on that evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that, as of March 31, 2017, our disclosure controls and procedures were effective at a reasonable level of assurance.

Changes in Internal Control over Financial Reporting

We concluded that there have been no changes in our internal control over financial reporting that occurred during the three months ended March 31, 2017, that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) of the Exchange Act).

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

The following information updates and amends the information provided in our Form 10-K in Part I, Item 3—Legal Proceedings. Capitalized terms used but not otherwise defined herein have the meanings set forth in our Form 10-K.

Alternative Water Supply in Lieu of Carmel River Diversions

Regional Desalination Project Litigation

On January 5, 2017, the parties to the consolidated action in San Francisco County Superior Court associated with the failure of the RDP participated in a CPUC-sponsored mediation that was unsuccessful in resolving the claims among them. On February 10, 2017, the Superior Court heard oral argument on the parties' demurrers to certain of the claims raised in this litigation. On February 14, 2017, the court issued an order sustaining in part and overruling in part the demurrers. On March 1, 2017, the parties to this litigation, other than RMC, filed amended pleadings and a schedule for filing additional motions has been set.

California Public Utilities Commission Residential Rate Design Proceeding

In December 2016, the California Public Utilities Commission (the "CPUC") issued a final decision in a proceeding involving California-American Water Company, the Company's wholly owned subsidiary ("Cal Am"), adopting a new residential rate design for Cal Am's Monterey District. The decision allowed for recovery by Cal Am of \$32 million in under-collections in the water revenue adjustment mechanism/modified cost balancing account (the "WRAM/MCBA") over a five-year period, plus interest, and modified existing conservation and rationing plans. In its decision, the CPUC noted concern regarding Cal Am's residential tariff administration, specifically regarding the lack of verification of customer-provided information about the number of residents per household. This information was used for generating billing determinants under the tiered rate system. As a result, the CPUC kept this proceeding open to address several issues, including whether Cal Am's residential tariff administration violated a statute, rule or CPUC decision, and if so, whether a penalty should be imposed.

On February 24, 2017, Cal Am, the Monterey Peninsula Water Management District, the CPUC's Office of Ratepayer Advocates, and the Coalition of Peninsula Businesses filed for CPUC approval of a joint settlement agreement (the "Joint Settlement Agreement"), which among other things, proposed to resolve the CPUC's residential tariff administration concerns by providing for a waiver by Cal Am of \$0.5 million of cost recovery for residential customers through the WRAM/MCBA in lieu of a penalty. Approval of the Joint Settlement Agreement, which is required for it to take effect, remains pending before the CPUC.

On March 28, 2017, the administrative law judge assigned to the proceeding issued a ruling stating there was sufficient evidence to conclude, on a preliminary basis, that Cal Am's administration of the residential tariff violated certain provisions of the California Public Utilities Code and a CPUC decision. The ruling ordered Cal Am to show cause why it should not be penalized for these administrative violations and directed the settling parties to address whether the cost recovery waiver in the Joint Settlement Agreement was reasonable compared to a potential penalty range described by the administrative law judge. During hearings held on April 13-14, 2017, the administrative law judge clarified that this potential penalty range is \$3.1 million to \$178.9 million (calculated as a continuing violation dating back to 2000 and applying penalties of up to \$20,000 per day until January 1, 2012 and penalties of up to \$50,000 per day thereafter, reflecting a 2012 change to the relevant statute). The administrative law judge also noted that a per diem penalty may not be appropriate, as Cal Am's monthly billing practices did not allow Cal Am to update customer-provided information for billing purposes on a daily basis. The administrative law judge has set further hearings in this proceeding for August 17, 2017, and has permitted certain of the parties, including Cal Am, to submit

additional written testimony on the issue of whether Cal Am should be penalized, and if so, the reasonable amount of any such penalty.

Cal Am believes that the terms of the Joint Settlement Agreement are fair and reasonable, that its residential tariff administration is compliant with California Public Utilities Code and it is able to assert credible defenses against the CPUC's allegations of wrongdoing and the associated penalties. Cal Am intends to vigorously defend itself in this proceeding against these allegations and the imposition of penalties; however, the ultimate outcome of this matter cannot be determined at this time.

West Virginia Elk River Freedom Industries Chemical Spill

Background

On July 7, 2016, the court in the Federal action scheduled trial to begin on October 25, 2016, but the court has granted several continuances of the trial, which is currently postponed until June 6, 2017 and remains subject to further delay in light of the proposed settlement agreement discussed below. The Mass Litigation Panel has also stayed its proceedings until July 26, 2017.

WVAWC Binding Global Agreement in Principle to Settle Claims

On April 27, 2017, the parties filed with the court in the Federal action a proposed settlement agreement providing details of the terms of the Settlement consistent with those described above. The parties also requested that the court in the Federal action grant preliminary approval of the Settlement. If and when preliminary approval of the Settlement is obtained, notice of the terms of the Settlement would then be provided to members of the settlement class. Following the notice period, the court in the Federal action would hold a fairness hearing to consider final approval of the Settlement.

Other Related Proceedings

On April 4, 2017, the CSB indicated that the implementation by the Company of source water protection activities resolved the first two parts of the CSB's recommendation. The CSB also noted that compliance by the Company with the third part of its recommendation is ongoing and that closure of this part is contingent upon completion of updated contingency planning for the Company's water utilities outside of West Virginia.

On March 16, 2017, the Lincoln County (West Virginia) Commission (the "LCC") passed a county ordinance entitled the "Lincoln County, WV Comprehensive Public Nuisance Investigation and Abatement Ordinance." The ordinance establishes a mechanism that Lincoln County believes will allow it to pursue criminal or civil proceedings for the "public nuisance" it alleges was caused by the Freedom Industries chemical spill. On April 20, 2017, the LCC filed a complaint in Lincoln County state court against WVAWC and certain other defendants not affiliated with the Company, alleging that the Freedom Industries chemical spill caused a public nuisance in Lincoln County. The complaint seeks an injunction against WVAWC that would require the creation of various databases and public repositories of documents related to this chemical spill, as well as further study and risk assessments regarding the alleged exposure by Lincoln County residents to the released chemicals. WVAWC believes that the lawsuit is without merit and intends to vigorously contest the claims and allegations raised in the complaint.

ITEM 1A. RISK FACTORS

In addition to the other information set forth in this report, you should carefully consider the factors discussed in Part I, Item 1A—Risk Factors in our Form 10-K, and in our other public filings, which could materially affect our business, financial condition or future results. There have been no material changes from risk factors previously disclosed in Part I, Item 1A—Risk Factors in our Form 10-K.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

In February 2015, the Board of Directors authorized an anti-dilutive stock repurchase program to mitigate the dilutive effect of shares issued through the Company's dividend reinvestment, employee stock purchase and executive compensation activities. The program allows the Company to purchase up to 10 million shares of its outstanding common stock over an unrestricted period of time in the open market or through privately negotiated transactions. The program is conducted in accordance with Rule 10b-18 of the Exchange Act, and, to facilitate these repurchases, the Company enters into Rule 10b5-1 stock repurchase plans with a third-party broker, which allow the Company to repurchase shares of its common stock at times when it otherwise might be prevented from doing so under insider trading laws or because of self-imposed trading blackout periods. Subject to applicable regulations, the Company may elect to amend or cancel the program or the stock repurchase parameters at its discretion to manage dilution.

The following table provides a summary of information about the shares of common stock purchased by the Company during the three months ended March 31, 2017:

	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs (b)	Average Price Paid per Share (a)	Total Number of Shares Purchased	Maximum Number of Shares Available to be Purchased Under the Plan or Program
January 1 - January 31, 2017	—	—	—	6,750,000
February 1 - February 28, 2017	—	—	—	6,750,000
March 1 - March 31, 2017	700,000	\$ 77.44	700,000	6,050,000
Total	700,000	\$ 77.44	700,000	

(a) Average price paid per share includes brokerage fees and commissions incurred by the Company in connection with these repurchases.

(b) From April 1, 2015, the date repurchases under the anti-dilutive stock repurchase program commenced, through March 31, 2017, the Company repurchased an aggregate of 3,950,000 shares of common stock under the program.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. MINE SAFETY DISCLOSURES

None.

ITEM 5. OTHER INFORMATION

None.

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ITEM 6. EXHIBITS

Exhibit

Number Exhibit Description

- 3.1 Restated Certificate of Incorporation of American Water Works Company, Inc. (incorporated by reference to Exhibit 3.1 to the Company's Quarterly Report on Form 10-Q, File No. 001-34028, filed November 6, 2008).
- 3.2 Amended and Restated Bylaws of American Water Works Company, Inc. (incorporated by reference to Exhibit 3.2 to the Company's Quarterly Report on Form 10-Q, File No. 001-34028, filed August 5, 2015).
- *10.1.1 American Water Works Company, Inc. 2007 Omnibus Equity Compensation Plan 2017 Restricted Stock Unit Grant.
- *10.1.2 American Water Works Company, Inc. 2007 Omnibus Equity Compensation Plan 2017 Restricted Stock Unit Grant (for certain executives).
- *10.2.1 American Water Works Company, Inc. 2007 Omnibus Equity Compensation Plan 2017 Performance Stock Unit Grant Form A-1.
- *10.2.2 American Water Works Company, Inc. 2007 Omnibus Equity Compensation Plan 2017 Performance Stock Unit Grant Form A-2.
- *10.2.3 American Water Works Company, Inc. 2007 Omnibus Equity Compensation Plan 2017 Performance Stock Unit Grant Form B-1.
- *10.2.4 American Water Works Company, Inc. 2007 Omnibus Equity Compensation Plan 2017 Performance Stock Unit Grant Form B-2.
- *31.1 Certification of Susan N. Story, President and Chief Executive Officer, pursuant to Section 302 of the Sarbanes-Oxley Act.
- *31.2 Certification of Linda G. Sullivan, Executive Vice President and Chief Financial Officer, pursuant to Section 302 of the Sarbanes-Oxley Act.
- **32.1 Certification of Susan N. Story, President and Chief Executive Officer, pursuant to Section 906 of the Sarbanes-Oxley Act.
- **32.2 Certification of Linda G. Sullivan, Executive Vice President and Chief Financial Officer, pursuant to Section 906 of the Sarbanes-Oxley Act.
- *101 The following financial statements from American Water Works Company, Inc.'s Quarterly Report on Form 10-Q for the quarterly period ended March 31, 2017, filed with the Securities and Exchange Commission on May 3, 2017, formatted in XBRL (eXtensible Business Reporting Language): (i) the Consolidated Balance Sheets; (ii) the Consolidated Statements of Operations; (iii) the Consolidated Statements of Comprehensive Income; (iv) the Consolidated Statements of Cash Flows; (v) the Consolidated Statements of Changes in

Stockholders' Equity; and (vi) the Notes to Consolidated Financial Statements.

* Filed herewith.

** Furnished herewith.

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Signatures

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized, on the 3rd day of May, 2017.

AMERICAN WATER WORKS COMPANY, INC.
(REGISTRANT)

By /s/ SUSAN N. STORY
Susan N. Story

President and Chief Executive Officer

(Principal Executive Officer)

By /s/ LINDA G. SULLIVAN
Linda G. Sullivan

Executive Vice President and Chief Financial Officer

(Principal Financial Officer)

By /s/ MELISSA K. WIKLE
Melissa K. Wikle

Vice President and Controller

(Principal Accounting Officer)

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Income; (iv) the Consolidated Statements of Cash Flows; (v) the Consolidated Statements of Changes in Stockholders' Equity; and (vi) the Notes to Consolidated Financial Statements.

* Filed herewith.

**Furnished herewith.